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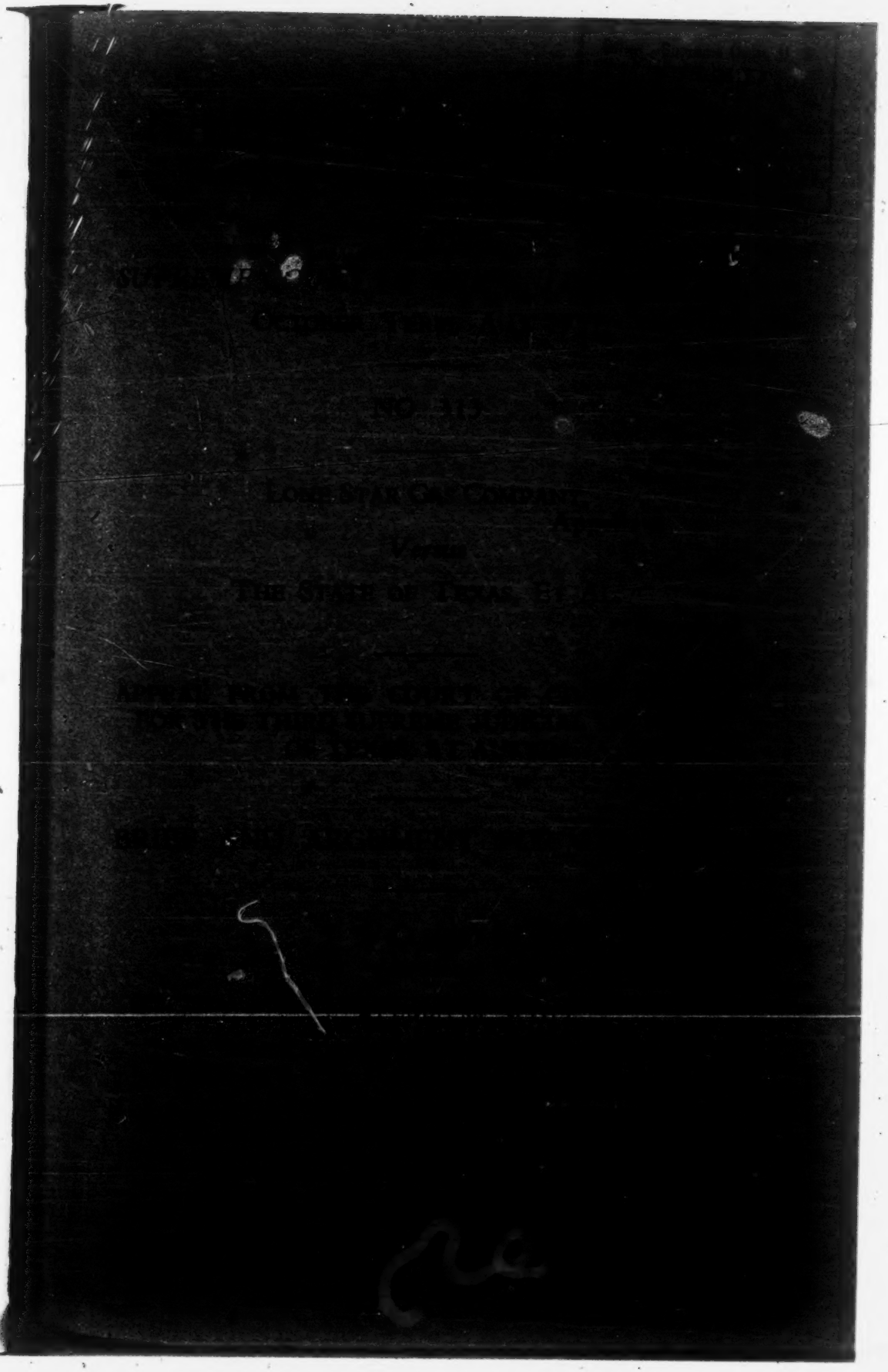

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IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, A.D. 1937

NO. 313

LONE STAR GAS COMPANY,
Appellant

Versus

THE STATE OF TEXAS, ET AL,
Appellees

APPEAL FROM THE COURT OF CIVIL APPEALS FOR THE THIRD SUPREME JUDICIAL DISTRICT OF TEXAS, AT AUSTIN

BRIEF AND ARGUMENT FOR APPELLEES

INTRODUCTORY STATEMENT

The Company's contentions are, in their essence, but a challenge to the entire rate regulatory power of the State. The Company has chosen to make this case a war, to see which is the more powerful—the Company or the State. We have accepted the gage of battle upon that basis. The future of rate regulation in Texas depends upon the outcome.

Appellant has tersely set forth only such facts as it deems favorable to it; and in the light most favorable to it. The brief consists in part of half-truths, and on occasion, of affirmative mis-statement.

That method of briefing would be admirably adapted to Appellant's purpose, if such purpose were to present the case to this Honorable Court in a distorted and misleading light. The overall effect of the brief is to place upon Appellees the burden not only of briefing their own side of the case in the usual way, but of undoing the affirmatively and prejudicially erroneous work of Appellant. If Appellant were to be permitted to gain the natural advantage of such method, whether deliberately adopted or not, the net result would be to shift the well established legal burden from Appellant of showing by "clear and convincing evidence" that it is a victim of confiscation or has been deprived of other federal constitutional rights, and illegally to place upon Appellees the burden of sustaining the legality and non-confiscatory character of the order by evidence and other demonstration of their own.

Appellees do not wish to have such an unlawful and unjust onus placed upon them, though they are confident they could sustain it under compulsion; and they hope that this Honorable Court will hold Appellant strictly to the discharge of the burden which devolves upon it by law.

Nevertheless, Appellees wish to be of as much help to the Court in arriving at a correct decision of the case as may be possible to do.

As affirmatively appears in the record, the hearings before the Commission lasted almost continuously for a period of about seven months; and the record made before that body was considerably more voluminous

than the record before the District Court, which has been somewhat diminished in printing. (R. I, 16).

At the trial in the District Court Appellees proffered in evidence the entire record made before the Commission, including all oral testimony and exhibits, but upon the Company's objections thereto the trial court excluded it, and it went up with the record on appeal as a bill of exceptions and is now to be found *in toto* in the original typewritten record in this Court. It was at the insistence of Appellees that the stipulation was made (R. V, 3485-3487) that the entire original appellate record should be brought to this Court in lieu of the usual transcript, so that this Court might have access to the entire record if it wishes. In filing printing praecipes in this Court Appellant was very insistent that no part of the Commission record should be printed.

We desire to make plain our attitude upon this point, however: that if this Court discovers any necessity, or feels any desire, to examine the whole or any part of the Commission record, or any portion of the District Court record which was not printed, we not only willingly invite the Court to do so, but will if necessary have the desired additional portions of the record printed even yet. We are not only willing, but anxious, that the Court read and consider the whole of the printed record, and such remaining parts of the unprinted record as it sees fit.

Appellant's brief in a large part is addressed to attacks upon the *reasoning* of the Court of Civil Appeals in its opinion. The judgment of the Supreme Court of Texas, affirming upon its merits the judg-

ment of the Court of Civil Appeals, by the refusal of a writ of error,[1] is totally ignored. This Court reviews and corrects errors in federal questions committed only in the *judgments* of courts below, and not mere errors of reasoning in their opinions. Our contention is that the judgment rendered by the Court of Civil Appeals, and affirmed by the Supreme Court of Texas, was a correct one upon this record, irrespective of whether or not the *rationale* by which they arrived at their conclusions and judgments was in all respects irrefragible and above criticisms.

In Appellant's preliminary statement of the case, (p. 4 of its brief) it points out that all except two of the distributors to whom it sells in Texas are its own affiliates; but it very carefully omits to point out that Appellant itself also distributes gas in retail directly to approximately 33,000 domestic consumers in the important city of Fort Worth, Texas, (R. I, 15, 219, 388; R. III, 1896; R. V, 3288A, "Fort Worth Division") and also makes extensive domestic, commercial and industrial sales directly to the consumers along the rights of way all over its system as well as in the "Fort Worth Division" of Lone Star Gas Company.

DIVISION A

INTERSTATE COMMERCE

I. In all proceedings before the Commission Appellant made not the slightest objection or suggestion that the Commission, because of the claimed self-

[1]Gammel-Statesman Pub. Co. vs. Ben C. Jones & Co., 206 S. W. 931.

enacting force of the commerce clause of the federal constitution, had no power to fix a uniform gate rate applicable to all gas delivered by Appellant's pipe line system at all points served by it in Texas, but deliberately lay in ambush for the Commission and by its premeditated silence and acquiescence permitted the Commission to make such a gate rate without the slightest hint of the claimed defense of interstate commerce, and Appellant is now thereby estopped to assert such attack or defense in any form for the first time in a judicial review of the Commission's order:

B. & O. R. Co. vs. United States, 298 U. S. 349, 392, 80 L. Ed. 1209;
Western Dist. Co. vs. Pub. Serv. Comm. of Kans. 58 Fed. (2d) 241, 243, (aff. 285 U. S. 119, 76 L. Ed. 655);
St. Joseph Stockyards Co. vs. United States 298 U. S. 38, 47-48, 53-54, 80 L. Ed. 1033;
Manufacturers R. Co. vs. United States, 246 U. S. 457, 470, 488-490, 62 L. Ed. 831;
C. N. O. & T. P. Ry. Co. vs. Interstate Commerce Commission, 162 U. S. 184, 196, 40 L. Ed. 935.

II. Distribution of natural gas to local consumers in Texas is intrastate commerce, and of local concern only, even though the supply, in whole or in part, be transported across state lines:

East Ohio Gas Co. vs. Tax Commission of Ohio, 283 U. S. 465, 470-471, 75 L. Ed. 1171, 1175;
Western Distributing Co. vs. Pub. Serv. Com. of Kans., 285 U. S. 119, 124-125, 76 L. Ed. 655, 658;

Pub. Ut. Com. of Kans. vs. Landon, 249 U. S. 236, 245, 63 L. Ed. 577, 586;
Dayton P. & L. Co. vs. Pub. Ut. Com. of Ohio, 292 U. S. 290, 306-308, 78 L. Ed. 1267, 1279;
Columbus G. & F. Co. vs. Pub. Ut. Com. of Ohio, 292 U. S. 398, 399-401, 78 L. Ed. 1327;
Manufacturers L. & H. Co. vs. Ott, 215 Fed. 940, 944-945.

III. The Commission has undoubted power, effectually and for all *practical* purposes, to determine and fix in burner tip cases the gate rate to be *charged and collected* for natural gas by transmission companies to distributors, even though the supply be in whole or in part transported across state lines, by the circuitous process of conducting in each burner tip case a hearing upon the transmission phase of the business, and fixing the maximum charge which the distributors may set up as an operating expense for gas purchases at the city gates. The fixing of a maximum operating expense for gate purchases for the distributors is in practical effect the same as directly fixing the charge to be made by the pipe line company. This is true both as to independent and affiliated distributors, for reasons more fully pointed out hereinafter.

Western Distributing Co. vs. Pub. Serv. Com. of Kansas, 285 U. S. 119, 124-125, 76 L. Ed. 655, 658;
Dayton P. & L. Co. vs. Pub. Ut. Com. of Ohio, 292 U. S. 290, 306-308, 78 L. Ed. 1267, 1279;

Columbus G. & F. Co. vs. Pub. Ut. Com. of Ohio, 292 U. S. 398, 399-401, 414-415, 78 L. Ed. 1327;
United Fuel Gas Co. vs. R. R. Com. of Ky., 278 U. S. 300, 320-321, 73 L. Ed. 390, 401.

IV. The Court of Civil Appeals and the Supreme Court of Texas properly disregarded the corporate fictions and treated the Lone Star group of affiliated companies as being in legal contemplation one integrated system or operating unit engaged in operating, under one common ownership, management and control, all phases of the natural gas business, to-wit. purchasing, producing, transporting, and distributing locally natural gas to the consumers at the burner tips in Texas:

Chicago, etc. Ry. Co. vs. Minneapolis Civic Assn., 247 U. S. 490, 498, 500-502, 62 L. Ed. 1229;
United States vs. Delaware L. & W. Ry. Co., 238 U. S. 516, 529, 59 L. Ed. 1438;
United States vs. Lehigh Valley Ry. Co., 220 U. S. 257, 273-274, 55 L. Ed. 458;
McCaskill Co. vs. United States, 216 U. S. 504, 514-515, 54 L. Ed. 590;
Davis vs. Alexander, 269 U. S. 114, 117, 70 L. Ed. 186;
United States vs. Reading Co., 253 U. S. 26, 57-63; 64 L. Ed. 760;
Northern Securities Co. vs. United States, 193 U. S. 197, 341, 48 L. Ed. 679, 702;
United States vs. Union Pac. Ry. Co., 226 U. S. 61, 88, 89, 57 L. Ed. 124, 134;
Southern Pac. Terminal Co. vs. Interstate Commerce Commission, 219 U. S. 498, 521-522, 55 L. Ed. 310;
Central Vermont Ry. Co. vs. Southern N. E. R. Corp., 1 Fed. Suppl. 1004, 1005, 1006;

Wabash Ry. Co. vs. American Refg. Trans. Co., 7 Fed. (2) 335, 343-345;
Gallatin Nat. Gas Co. vs. Pub. Serv. Com. of Mont., 79 Mont. 269, 256 Pac. 373, 377, 378.

V. When the corporate fictions are disregarded and the system considered as an integrated whole, under common ownership, management and control, as was properly done herein, the situation is the same as if production (or purchase), transportation, and distribution were actually all conducted under a common ownership, management and operation; and all such operations are subject to state regulation even though the gas in whole or in part be imported from other states:

Authorities cited under Points II and III, above, and
Pa. Gas Co. vs. Pub. Serv. Com. of N. Y., 252 U. S. 23, 64 L. Ed. 434;
Western Dist. Co. vs. Pub. Serv. Com. of Kans., 285 U. S. 119, 76 L. Ed. 655;
Dayton P. & L. Co. vs. Pub. Ut. Com. of Ohio, 292 U. S. 290, 78 L. Ed. 1267;
Columbus G. & F. Co. vs. Pub. Ut. Com. of Ohio, 292 U. S. 398, 399-401, 78 L. Ed. 1327;
United Fuel Gas Co. vs. Ry. Com. of Ky., 278 U. S. 300, 320-321, 73 L. Ed. 390;
East Ohio Gas Co. vs. Tax Com. of Ohio, 283 U. S. 465, 75 L. Ed. 1171;
Peoples Gas Co. vs. Pub. Serv. Com. of Penn., 270 U. S. 550, 70 L. Ed. 726;
Manufacturers L. & H. Co. vs. Ott, 215 Fed. 940, 944-945.

VI. The result, and the only result, which the Commission intended and accomplished in promul-

gating the order, was to establish a compensatory and reasonable gate rate for application to all domestic gas delivered by Appellant at the cities and towns in Texas (approximately 275 in number) served by Appellant's pipe line system; upon which gate rate have been and are to be founded in separate and subsequent proceedings and orders the domestic burner tip rates for such towns. Approximately 125 of such domestic burner tip cases were pending before the Commission when it initiated its investigation, (R. I, 15). It is the plan and purpose of the Commission in all pending and subsequent burner tip cases involving such cities and towns to treat the present gate rate order as being final, binding, and conclusive, upon all distributors and others at interest, as to the price which Appellant may charge and collect from the distributors, and which the distributors may pay Appellant and set up on their books as an operating expense for gas purchases to be covered into their burner tip rates; thus obviating the necessity of fixing the gate rate over in a separate proceeding in each of the 275 burner tip cases at prohibitive and needless expense. Under the cases cited above under Points II and III, the fixation of such a gate rate is an essential step necessarily involved in the ultimate fixation of burner tip rates, and must be accomplished either directly or indirectly at some stage of the admittedly intrastate function of gas rate regulation as a whole, in order to arrive ultimately at reasonable burner tip rates. Under the state law, the Commission is not required to exhaust its entire jurisdiction in one proceeding and order, but it may lawfully accomplish the process of regulation by piece-

meal,[2] as it has started out to do in this case, by fixing the price which may be charged at the wellhead,[3] and the amount to be charged at the city gates,[4] and in separate and subsequent proceedings based upon the previously fixed wellhead and gate rates it may finally fix the ultimate burner tip rates,[4] either in the exercise of its original jurisdiction possessed concurrently with the incorporated cities and towns (see Art. 1119 as amended, quoted in appendix to Appellant's original brief) and under Arts. 6050-6059,[5] or its appellate jurisdiction on appeal from action of the cities under Art. 6058,[5] as done in *United Gas Pub. Serv. Co. vs. State,* 89 S. W. (2d) 1094, writ refused, affirmed by this Court Feb. 14, 1938, No. 13. So far as federal constitutional questions are concerned (which only are of interest to this Court) we must consider only the question whether, consistently with the federal commerce clause, the Commission may directly dispose of the production and transmission phases in one proceeding and order, as it has done here, as an indispensable step in the process of ultimate local burner tip regulation, or whether under the federal commerce clause it must accomplish identically the same ultimate result indirectly by trying the production and transmission phases in each of

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[2]Houston Chamber of Commerce vs. R. R. Com. of Tex., 19 S. W. (2d) 583, 586, aff. 78 S. W. (2d) 591.

[3]R. R. Com. of Tex. vs. Humble O. & R. Co., 101 S. W. (2d) 614.

[4]State of Texas vs. Pub. Serv. Corpn. of Tex., 88 S. W. (2d) 627, writ ref.

[5]See appendix at end of this brief.

approximately 275 burner tip cases. Nothing in the letter or spirit of the federal commerce clause can reasonably be interpreted as prohibiting the pursuit of the first-mentioned course in the circumstances shown by this record. The federal commerce clause has not such self-enacting force that it precludes all state legislation affecting interstate commerce. The question of whether it precludes particular state regulation is not one for the judiciary but for the Congress.[6] The substance and not the form should be controlling. The important thing from the standpoint of the federal commerce clause is the substantial effect of the state regulation upon interstate commerce, and not the mere means by which the ultimate result is reached. There is no substantial difference, so far as the essential ultimate effect of the gate rate order upon interstate commerce is concerned, between the Commission's order here, and the situation as it would stand if the Commission should conduct 275 separate burner tip hearings, and in each case try the production and transmission phases over. If the essential ultimate result can be attained by the Commission through the indirect method of prescribing maximum gate rates for gas purchases by the distributors in burner tip cases, (and Appellant admits that this may be done, R. V, 3500-3501) then certainly the same end may be lawfully reached by the more expeditious and economical direct method here employed. The result ultimately to be obtained, and the essential

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[6]South Carolina State Highway Dept. vs. Barnwell Bros., ... U. S. ..... 82 L. Ed. ..... (No. 161, Oct. Term, 1937, Feb. 14, 1938, Adv. Op. L. Ed. No. 10, 469, 473-477).

effect thereof upon interstate commerce, are identically the same in each instance. If the distributors be affiliated, the money all goes into and comes out of the same pocket anyway—that of the holding company, Lone Star Gas Corporation. If the distributors be non-affiliated they cannot long avoid financial ruin if they continue to pay more at the gate than they can cover into their rates; so in either event the amount fixed as the gate rate is for all practical purposes controlling as to the amount to be realized at the gate for the gas.

VII. Since the only "commerce" in which the integrated Lone Star system engages in Texas is the intrastate business of serving natural gas to the ultimate consumers at the burner tips (the corporate fictions being disregarded); and since such transportation of gas across state lines as occurs is purely an incident of such local commerce; the mere transportation by Appellant of its own gas across state lines into Texas, whether from Oklahoma or the Texas Panhandle field, for the sole purpose of there selling same in intrastate local distribution to Texas consumers, is not interstate commerce, but is only an incident of local commerce. Mere transportation, across state lines, of a commodity by its owner does not, of itself and abstractly considered, constitute "commerce" at all—much less "interstate commerce"—but the characterization of that transportation as an incident of interstate or intrastate commerce is conditioned by and depends solely upon what kind of "commerce" the owner is going to engage in with the commodity when it arrives at its destination in the receiving State:

United States vs. Ohio Oil Co. (the Pipe Line Cases), 234 U. S. 548, 561-562, 58 L. Ed. 1459, 1471;
Pa. R. R. Co. vs. Pub. Serv. Com. of Ohio, 298 U. S. 170, 80 L. Ed. 1130;
Pa. Gas Co. vs. Pub. Serv. Com. of N. Y., 252 U. S. 23, 64 L. Ed. 434;
Dayton P. & L. Co. vs. Pub. Ut. Com. of Ohio, 292 U. S. 290, 78 L. Ed. 1267;
Western Dist. Co. vs. Pub. Serv. Com. of Kans., 285 U. S. 119, 76 L. Ed. 655;
East Ohio Gas Co. vs. Tax Commission of Ohio, 283 U. S. 465, 75 L. Ed. 1171;
United Fuel Gas Co. vs. R. R. Com. of Ky., 278 U. S. 300, 320-321, 73 L. Ed. 390;
Manufacturers L. & H. Co. vs. Ott, 215 Fed. 940, 944-945;
State ex rel Caster vs. Flannelly, 96 Kans. 372, 152 Pac. 22, 26-27;
W. Va. & Md. Gas Co. vs. Towers, 134 Md. 137, 106 Atl. 265, 267-269.

VIII. The gas transported through Line A from the Panhandle field in Wheeler County, Texas, across the southwest corner of Oklahoma and back into Texas for local Texas consumption is not *inherently* interstate commerce, but is in fact and in law essentially intrastate commerce, since both termini are in Texas. Whether its regulation is potentially within reach of congressional action as a part of the "current of interstate commerce," (see *Minnesota vs. Blasius*, 290 U.S. 1, 78 L. Ed. 131) is immaterial:

Lehigh Valley R. R. Co. vs. Pa., 145 U. S. 192, 201-202, 36 L. Ed. 672;
U. S. Express Co. vs. Minn., 223 U. S. 335, 341-342, 56 L. Ed. 459;

Ewing vs. City of Leavenworth, 226 U. S. 464, 467, 57 L. Ed. 303;
United States vs. Powers Co., 211 Fed. 169.

IX. The transportation of gas through Line A from the Panhandle field in Wheeler County, Texas, across the southwest corner of Oklahoma and back into Texas for local Texas consumption is not in fact or in law interstate commerce, in the circumstances revealed by this record, because the evidence plainly shows that there was no necessity or justification for running Line A into the State of Oklahoma, but the same could more economically and profitably have been laid entirely within Texas, and the placing of a short section of this line parallel to, and barely within, the Oklahoma line in barren country (destitute of markets except for Hollis, Oklahoma, which could more economically have been served by a tap line extending from a main line in Texas) and when Wellington, Texas, (a larger town than Hollis, Okla.) could have been served by such Texas line, was merely a fraudulent subterfuge or device for the purpose of giving the appearance of interstate commerce to that which in its essence is not such, and for the purpose of evading the lawful regulatory power of the Texas Commission:

Sprout vs. South Bend, 277 U. S. 163, 168, 72 L. Ed. 833;
Interstate Buses vs. Holyoke St. Ry. Co., 273 U. S. 45, 71 L. Ed. 530;
Austin vs. Tenn., 179 U. S. 343, 359-360, 45 L. Ed. 224;
B. & O. S. W. Ry. Co. vs. Settle, 260 U. S. 166, 168-169; 67 L. Ed. 189;

Inter-City Coach Co. vs. Atwood, 21 Fed. (2d) 83;
Fed. Trade Com. vs. Smith, 1 Fed. Suppl. 247, 253.

X. As to the relatively small and rapidly diminishing volume of Oklahoma-produced gas transported into Texas, the record shows obviously that this gas is unnecessarily imported, it being undisputed and indisputable that there is much more than ample Texas gas available to Appellant from its own reserves and from its existing and potential purchase connections in Texas to meet all of its Texas demands; and, further, that the Oklahoma-produced gas costs Appellant from 6 to 15 cents per MCF in Oklahoma, plus the cost of transportation to Texas, whereas the Texas gas can be bought in unlimited quantities for from 2 to 6 cents per MCF.

The continued importation of such small volumes of Oklahoma gas, and the interposition of such importations under the claimed defense of interstate commerce, are therefore only obviously fraudulent subterfuges to avoid state regulation in Texas.

Peoples Nat. Gas Co. vs. Pub. Serv. Com. of Pa., 270 U. S. 550, 70 L. Ed. 726;
Sprout vs. South Bend, 277 U. S. 163, 168; 72 L. Ed. 833;
Interstate Buses vs. Holyoke St. Ry. Co., 273 U. S. 45, 71 L. Ed. 530;
Austin vs. Tenn., 179 U. S. 343, 359-360, 45 L. Ed. 224;
B. & O. S. W. Ry. Co. vs. Settle, 260 U. S. 166, 168-169; 67 L. Ed. 189;

Inter-City Coach Co. vs. Atwood, 21 Fed. (2d) 83;
Fed. Trade Com. vs. Smith, 1 Fed. Suppl. 247, 253.

XI. As to the relatively small and rapidly diminishing volume of Oklahoma-produced gas transported into Texas, the record shows that the greater part of such volume is returned to Oklahoma in kind from Texas gas, and in the segregation between Texas and Oklahoma properties and operations made by the Commission in the District Court the small excess of Oklahoma-produced gas transported into Texas over the Texas gas transported into Oklahoma is adequately compensated for by the allowance of the average prevailing Texas sales price for gas, thus giving the Oklahoma gas virtually "free transportation" to Texas. The Company's evidence shows that the gas flows alternately in each direction across the Texas-Oklahoma line and throughout the system. In reality, therefore, this is but a temporary borrowing or exchange of gas between portions of Appellant's system located in the two States, adopted of the Appellant's own volition, for its own operating convenience, if not for fraudulent purposes, and is not interstate commerce.

XII. The amount of Oklahoma-produced gas transported into Texas, or at least the excess of such Oklahoma importations over Texas gas transported into Oklahoma, as compared with the total amount of gas sold on the Lone Star system in Texas, is so unsubstantial and negligible in amount, that it should be disregarded under the rule of *de minimis lex non curat;* especially since the record shows undisputably

that such importations, already small at the time of the District Court trial, were and are sharply and steadily declining, and have now probably reached the vanishing point; and in view of the fact that Appellants own testimony showed (R. II, 1417) that Line H was to be (and it actually has been) removed in 1934; so that now probably more Texas gas is transported to Oklahoma than vice-versa.

XIII. Since the evidence showed without dispute that Appellant owns ample gas reserves in Texas, and can easily and cheaply acquire unlimited additional gas reserves and gas purchase connections in Texas, to supply all of its actual and potential Texas demands for many years to come, the order does not require Appellant to use in Texas any gas imported from Oklahoma or elsewhere; and all of Appellant's Texas deliveries should therefore be treated as if they were Texas gas. If Appellant sees fit voluntarily to use in Texas any gas imported from Oklahoma in lieu of the ample Texas gas available, Appellant thereby subjects the same to Texas control:

Peoples Natural Gas Co. vs. Pub. Serv. Com. of Penn., 270 U. S. 550, 70 L. Ed. 726.

XIV. The order does not in any way prohibit, restrict, impede, or directly burden, the free importation or exportation of gas from state to state, nor does it discriminate against foreign gas in favor of Texas gas, but leaves the gas free to flow unrestrictedly both ways across the state line, and leaves all foreign and Texas gas upon an absolute equality of footing in Texas:

Sonneborn vs. Cureton (Keeling), 262 U. S. 506, 513-514, 67 L. Ed. 1095;
Peoples Nat. Gas Co. vs. Pub. Serv. Com. of Penn., 270 U. S. 550, 70 L. Ed. 726;
Penn. Gas Co. vs. Pub. Serv. Com. of N. Y., 252 U. S. 23, 64 L. Ed. 434;
Western Distr. Co. vs. Pub. Serv. Com. of Kans., 285 U. S. 119, 124-125, 76 L. Ed. 655;
Dayton P. & L. Co. vs. Pub. Ut. Com. of Ohio, 292 U. S. 290, 306-308, 78 L. Ed. 1267, 1279;
United Fuel Gas Co. vs. R. R. Com. of Ky., 278 U. S. 300, 320-321, 73 L. Ed. 390, 401;
East Ohio Gas Co. vs. Tax Commission of Ohio, 283 U. S. 465, 470-471, 75 L. Ed. 1171-1175;
Manufacturers L. & H. Co. vs. Ott, 215 Fed. 940;
The instant case is to be distinguished from:
West vs. Kans. Nat. Gas Co., 221 U. S. 229, 55 L. Ed. 716;
Penn. vs. W. Va., 262 U. S. 553, 67 L. Ed. 1117.

XV. Even if it be conceded (as it is not) that both the Oklahoma-produced gas and the gas from the Panhandle field in Wheeler County, Texas, are transported in interstate commerce, yet the effect of the present order establishing a gate rate for application within Texas, is not a prohibited, direct and substantial burden upon interstate commerce, but has at most only an unprohibited, indirect, remote, unsubstantial, and incidental effect upon interstate commerce; and the fixation of such a gate rate, even applied to all the gas sold in Texas by Appellant, is within the legal power of the Texas Commission as one of the indispensable steps toward the exercise of its undoubted power to

fix reasonable ultimate burner tip rates even upon gas transported across state lines:

South Carolina Highway Dept. vs. Barnwell Bros., ____ U. S. ____, 82 L. Ed. ____, (No. 161, Oct. Term, 1937, Feb. 14, 1938, L. Ed. Adv. Op. No. 10, 469, 473-477);

Washington ex rel. Foss vs. Kelly, ____ U. S. ____, 82 L. Ed. ____, (L. Ed. Adv. Op. p. 39);

Natural Gas Pipe Line Co. vs. Slattery, No. 230, October Term, 1937, ____ U. S. ____, 82 L. Ed. ____, (L. Ed. Adv. Op. No. 5, p. 205);

James vs. Dravo Contracting Co., ____ U. S. ____, 82 L. Ed. ____ (No. 3, Oct. Term 1937, L. Ed. Adv. Op. No. 5, p. 125);

Silas Mason Company vs. Tax Comm. of Washington, ____ U. S. ____, 82 L. Ed. ____ (Nos. 7 & 8, Oct. Term, 1937, L. Ed. Adv. Op. No. 5, p. 154).

Southern Nat. Gas Corp. vs. Ala., 301 U. S. 148, 81 L. Ed. 970;

Western Distr. Co. vs. Pub. Serv. Com. of Kans., 285 U. S. 119, 124-125, 76 L. Ed. 655;

Dayton P. & L. Co. vs. Pub. Ut. Com. of Ohio, 292 U. S. 290, 306-308, 78 L. Ed. 1267;

United Fuel Gas Co. vs. R. R. Com. of Ky., 278 U. S. 300, 401, 73 L. Ed. 390;

East Ohio Gas Co. vs. Tax Commission of Ohio, 283 U. S. 465, 470-471, 75 L. Ed. 1171;

Pub. Ut. Com. of Kans. vs. Landon, 249 U. S. 236, 245; 63 L. Ed. 577;

Penn. Gas Co. vs. Pub. Serv. Com. of N. Y., 252 U. S. 23, 29-30, 64 L. Ed. 434;

Peoples Nat. Gas Co. vs. Pub. Serv. Com. of Penn., 270 U. S. 550, 70 L. Ed. 726;

Manufacturers L. & H. Co. vs. Ott, 215 Fed. 940, 944-945;

State ex rel Caster vs. Flannelly, 96 Kans. 372, 152 Pac. 22, 26-27;

W. Va. & Md. Gas Co. vs. Towers, 134 Md. 137, 106 Atl. 265, 267-269;
Ala. vs. Southern Nat. Gas Corp., 170 So. 178;
United States F. & G. Co. vs. Kentucky, 231 U.S. 394, 397, 399, 58 L. Ed. 283;
Simpson vs. Shepard (Minnesota Rate Cases), 230 U. S. 352, 402-431, 57 L. Ed. 1152;
Atlas Pipe Line Co. vs. Sterling, 4 Fed. Suppl. 441;
Schechter Poultry Corp. vs. United States, 295 U. S. 495, 544-551, 79 L. Ed. 1570;
Munn vs. Illinois, 94 U. S. 113, 135, 24 L. Ed. 77;
State Tax on Railway Gross Receipts, 15 Wall. 284, 293, 294, 21 L. Ed. 167;

XVI. Considering the fact that when the gas leaves the Wheeler County field in Texas, and the various fields in Oklahoma, its destination is not known or determined in advance, and the fact that the same is, after arrival in Texas, shifted at the will of Appellant to whatever destination may suit its own whim and fancy, thus enabling Appellant by playing fast and loose through such continuous shifting, to defeat regulation by all competent authorities, both State and Federal; and the fact also that no orders are placed for, or sales made of, the gas before its entry into Texas, and no sale of any specific or particular identifiable volume thereof is ever made even after entry into Texas, but that in a part of the system's territory the same is drawn off from the mixture of Texas and Oklahoma gas only upon demand of, and as needed by, the affiliated distributors and the Texas consumers (including those in the Fort Worth Division) to whom it is ultimately sold, such Texas Panhandle and

Oklahoma gas is not moving in interstate commerce when it reaches the city gates in Texas:

Sonneborn Bros. vs. Cureton (Keeling), 262 U.S. 506, 67 L. Ed. 1095.

XVII. Even if it be conceded (as it is not) that both the Oklahoma-produced gas and the gas from the Panhandle field in Wheeler County, Texas, are transported in interstate commerce in such circumstances as to be originally beyond the regulatory power of Texas, yet the treatment of such gas by Appellant in the following particulars, after the gas arrives in Texas, and before delivery to the distributors, constitutes a breaking of the original package, and a commingling and amalgamation of the gas with the general mass of property in Texas, and the bringing of the interstate movement to a rest and end, in such a way and to such extent as to deprive the same of its claimed original interstate character and exemption from state control; namely: in extracting therefrom the gasoline and other volatile hydro-carbons; changing the chemical content, specific gravity, and BTU heating content thereof; reducing the pressure of same (through regulators owned, maintained and operated by Appellant) from high pressures of 150 to 350 pounds to low pressures of 20 or 30 pounds per square inch before delivery to distributors and industrial customers in Texas; reducing the same to pressures even as low as 4 to 6 ounces before service to numerous rural right-of-way customers and to approximately 33,000 retail domestic, commercial, and industrial customers in the City of Fort Worth; the breaking up of the larger streams of such gas in the high pressure transmission lines into many smaller

streams and lower pressures in tap and lateral lines; the storing of large volumes of the Texas Panhandle and Oklahoma gas for long periods in the underground Miller farm near Petrolia, Texas; and the commingling of such claimed interstate gas with much larger volumes of admittedly intrastate gas in such way that the same cannot be, or at least has not been in this record, definitely measured, identified, and segregated by volume and source in such way that it can be ascertained at any particular city gate what portion, if any, of the total delivery at any particular time is from Oklahoma and what portion, if any, is from the Texas Panhandle Field.

Southern Natural Gas Corp. vs. State of Alabama, 301 U. S. 148, 81 L. Ed. 970;
State of Alabama vs. Southern Nat. Gas Corp., 170 Southern 178;
State ex rel. Caster vs. Flannelly, 96 Kans. 372;
South Carolina Power Co. vs. South Carolina Tax Com., 52 Fed. (2d) 515, 523-525, Aff. 286 U. S. 525, 76 L. Ed. 1268;
Sonneborn Bros. vs. Cureton (Keeling), 262 U.S. 506, 513, 522, 67 L. Ed. 1095;
Brown vs. Houston, 114 U. S. 622, 632-634, 29 L. Ed. 257;
Penn. Gas Co. vs. Pub. Serv. Com. of N. Y., 252 U. S. 23, 64 L. Ed. 434;
Peoples Nat. Gas Co. vs. Pub. Serv. Com. of Penn., 270 U. S. 550, 70 L. Ed. 726;
East Ohio Gas Co. vs. Tax Commission of Ohio, 283 U. S. 465, 75 L. Ed. 1171;
Dayton P. & L. Co. vs. Pub. Ut. Com. of Ohio, 292 U. S. 290, 78 L. Ed. 1267;
Western Distr. Co. vs. Pub. Serv. Com. of Kans., 285 U. S. 119, 76 L. Ed. 655;

Public Ut. Com. of Kans. vs. Landon, 249 U. S. 236, 63 L. Ed. 577;
May vs. New Orleans, 178 U. S. 496, 509-510, 44 L. Ed. 1165;
Amer. Steel & Wire Co. vs. Speed, 192 U. S. 500, 521-522, 48 L. Ed. 538;
Gulf Fisheries vs. McInerney, 276 U. S. 124, 72 L. Ed. 495;
Minn. vs. Blasius, 290 U. S. 1, 10-12, 78 L. Ed. 131;
Whitfield vs. Ohio, 297 U. S. 431, 438-440, 80 L. Ed. 778.
West Va. & Md. Gas Co. vs. Towers, 134 Md. 137, 106 Atl. 265, 267-269;

XVIII. Congress never having enacted any legislation toward regulating the interstate transportation of natural gas by pipe line, but having in the amendments to the Interstate Commerce Act expressly excepted that traffic from federal regulation, the undoubted congressional intent is evinced that this field of regulation shall be left to the respective states, in so far as same pertains to their local concerns. The fixing of a uniform gate rate for natural gas served by Appellant's pipe line system only to cities and towns in Texas, to the extent and in the circumstances shown by this record, only as a prelude and an indispensable step toward the fixing of ultimate burner tip rates in Texas, which the state has the undoubted power to fix, is not a subject of national character or concern requiring or even permitting convenient and practicable uniformity of regulation as between state and state, and it is, therefore, not forbidden to the state by the Commerce Clause of the Federal Constitution. This is a legislative matter in which the Congress alone has the power and discretion to determine as a legislative

policy (and not the courts as a judicial function) whether the states shall not be permitted to legislate, even though interstate commerce be affected. Texas is, therefore, left free to exercise regulatory control of that business by taking this necessary intermediate step toward fixing reasonable prices at which natural gas, even though imported from other States, may be sold to its own citizens in intrastate commerce to local consumers, this being a matter of local concern to Texas only, in no wise affecting Oklahoma or other states:

U. S. C. A. Tit. 49, Ch. 1, Sec. 1, Par. (1), Subdivision (b); (Interstate Commerce Act);

South Carolina State Highway Dept. vs. Barnwell Bros., ____ U. S. ____, 82 L. Ed, ____, (No. 161, Oct. Term, 1937, Feb. 14, 1938, L. Ed. Adv. Op. No. 10, 469, 473-477);

Kelly vs. Washington, ____ U. S. ____; 82 L. Ed. ____ (No. 2, Oct. Term, 1937, L. Ed. Adv. Op. No. 3, p. 39);

Townsend vs. Yeomans, 301 U. S. 441, 449, 450, 81 L. Ed. 1210, 1217, 1218;

James vs. Dravo Const. Co., ____ U. S. ____, 82 L. Ed. ____, (No. 3, Oct. Term, 1937, L. Ed. Adv. Op. No. 5, p. 125);

Silas Mason Co. vs. Tax Com. of Wash., ____ U. S. ____, 82 L. Ed. ____, (Nos. 7 and 8, Oct. Term, 1937, L. Ed. Adv. Op. No. 5, p. 154);

Penn. Gas Co. vs. Pub. Serv. Com. of N. Y., 252 U. S. 23, 29-31, 64 L. Ed. 434;

Northwestern Bell Tel. Co. vs. Nebraska St. Ry. Com., 297 U. S. 471, 477-480; 80 L. Ed. 810;

Simpson vs. Shepard (Minnesota Rate Cases), 230 U. S. 352, 399-400, 402, 431, 57 L. Ed. 1511;

Smith vs. Ill. Bell Tel. Co., 282 U. S. 133, 159-160, 75 L. Ed. 255;

Minn. vs. Blasius, 290 U. S. 1, 9, 78 L. Ed. 131;
Carter vs. Carter Coal Co., 298 U. S. 238, 297-307, 80 L. Ed. 1160;
Schechter Poultry Corp. vs. United States, 295 U. S. 495, 544-551, 79 L. Ed. 1570;
Bradley vs. Pub. Ut. Com. of Ohio, 289 U. S. 92, 95-96, 77 L. Ed. 1053;
Re State Tax on Railway Gross Receipts, 15 Wall. 293, 21 L. Ed. 167;
Escanaba & L. M. Transp. Co. vs. Chicago, 107 U. S. 678, 683, 687, 27 L. Ed. 442;
Smith vs. Alabama, 124 U. S. 465, 31 L. Ed. 508;
Hennington vs. Georgia, 163 U. S. 299, 317, 41 L. Ed. 166;
N. Y. N. H. & H. R. Co. vs. N. Y., 165 U. S. 628, 631, 41 L. Ed. 853;
Smyth vs. Ames, 169 U. S. 466, 522, 42 L. Ed. 819;
M. K. & T. Ry. Co. vs. Haber, 169 U. S. 613, 633-635, 42 L. Ed. 878;
Penn. R. R. Co. vs. Hughes, 191 U. S. 477, 487, 491, 48 L. Ed. 268;
Mo. Pac. Ry. Co. vs. Larabee Mills, 211 U. S. 612, 623, 53 L. Ed. 352;
Knott vs. C. B. & Q. R. Co. (Missouri Rate Cases), 230 U. S. 474, 496-497, 57 L. Ed. 1571;
Port Richmond & B. P. Ferry Co. vs. Board of Chosen Freeholders, 234 U. S. 317, 330, 58 L. Ed. 1330;
Sligh vs. Kirkwood, 237 U. S. 52, 61, 59 L. Ed. 835;
International Bridge Co. vs. N. Y., 254 U. S. 126, 132-133; 65 L. Ed. 176;
Morris vs. Duby, 274 U. S. 135, 143, 71 L. Ed. 966;

Sproles vs. Binford, 286 U. S. 374, 389-390, 76 L. Ed. 1167;
Manufacturers L. & H. Co. vs. Ott, 215 Fed. 940, 944-945;
State ex rel Caster vs. Flannelly, 96 Kans. 372, 152 Pac. 22, 27;

XIX. Appellant is shown to be engaged in intrastate activities in Texas to such extent as to subject it to the regulatory power of Texas in its entire business, in that it is engaged in substantial volumes of right-of-way retail sales of gas at reduced pressures to rural domestic customers; in the sale of gas at lowered pressures to numerous industries, many of them large, through tap lines, metering and regulating stations owned, operated, and maintained by Appellant at and on the properties of the industries; in the direct service, in retail distribution, of approximately 33,000 domestic, commercial, and industrial customers through local distribution properties, metering and regulating devices, owned, operated, and maintained by Appellant in the City of Fort Worth, Texas, in the maintenance of its general office building and principal place of business of the Lone Star group of affiliated companies in Dallas, Texas, where such group, including Appellant, receives and fills orders for gas, and other commodities and services handled by the group, issues checks in payment of all obligations, and carries on all of the general administration and other operations pertaining to the entire business of said affiliated group; and in the fact that through common stock ownership, affiliation, and control through common or interlocking directors, officials, and employees, both Appellant and its affiliated distributing companies are in reality the *alter*

egos of the Lone Star Gas Corporation (a Delaware holding company) engaged in local distribution in all Texas towns (approximately 275 in number) on the system, with the single exception of Gainesville:

Southern Nat. Gas Corp. vs. Alabama, 301 U. S. 148, 81 L. Ed. 970;
Alabama vs. Southern Nat. Gas Corp., 170 So. 178.

XX. Appellant having for the first time raised the claimed defense of interstate commerce before the District Court, and having made no such suggestion or defense before the Commission, this suggestion or claimed defense, (if same was to any extent well founded, which we do not concede), that some part of Appellant's properties and operations within Texas were exempt from Texas control, created for the first time, in the District Court, a necessity that a plain, definite, just, reasonable, and practical segregation as between Texas and Oklahoma properties and operations, and between that gas claimed by Appellant to be subject and not subject, respectively, to the regulatory control of Texas, should be made by Appellant, in order that both Texas and Oklahoma might justly and intelligently regulate those portions of Appellant's properties and business falling within their respective spheres of legislative regulation; and in order that Texas consumers might not be unjustly burdened by the more expensive intrastate operations in Oklahoma, and in order that the Commission might exempt from its order all gas, if any, properly beyond its regulatory control. In order to establish the defense, the burden of making such a segregation, and of supplying plain,

definite, and convincing evidence on which such a segregation could be made by the Commission and the reviewing courts, rested upon Appellant and not upon the Commission, and was not discharged by Appellant.

Norfolk & Western Ry. Co. vs. North Carolina, 297 U. S. 682, 688-689, 80 L. Ed. 977;
Smith vs. Ill. Bell Tel. Co., 282 U. S. 133, 146-151, 75 L. Ed. 255;
Simpson vs. Shepard (Minnesota Rate Cases), 230 U. S. 352, 435-436, 461, 465-466, 57 L. Ed. 1511;
Great Northern Ry. Co. vs. Weeks, 297 U. S. 135, 143-145, 80 L. Ed. 532;
Smyth vs. Ames, 169 U. S. 466, 540-542, 42 L. Ed. 819, 847;
Wabash Valley Elec. Co. vs. Young, 287 U. S. 488, 497-498, 77 L. Ed. 447;
Houston vs. S. W. Bell Tel. Co., 259 U. S. 318, 322, 66 L. Ed. 961, 964;
United Fuel Gas Co. vs. R. R. Com. of Ky., 278 U. S. 300, 73 L. Ed. 390.

XXI. It was not necessary that the Commission in its opinion and order make any express segregation between Texas and Oklahoma properties and operations, or between the gas subject to state regulation and that not so subject; especially in view of the fact that Appellant did not interpose any suggestion or claimed defense of interstate commerce before the Commission or submit any evidence upon which such segregations could be made; and it was, therefore, requisite only, and would have been sufficient, that Appellant (not Appellees) adduce before the District Court clear and satisfactory evidence which would have enabled that court and the appellate courts to make the necessary

segregation without the Commission having done so in its opinion and order. This latter burden was not discharged by Appellant:

Smith vs. Ill. Bell Tel. Co., 282 U. S. 133, 75 L. Ed. 255;
Lindheimer vs. Ill. Bell Tel. Co., 292 U. S. 151, 78 L. Ed. 1182.

XXII. Appellant did not discharge the burden which rested upon it under the law (if interstate commerce was directly burdened, which we deny) of making a reasonable, just, and practical segregation between Texas and Oklahoma properties and operations, or between the gas subject to state regulation and that claimed not to be so subject, either before the Commission or the District Court. Appellant made no suggestion or claimed defense of interstate commerce, and no segregation whatever, before the Commission; and before the District Court it made only a wholly untenable, unsound, impractical, unjustifiable, incomprehensible, unjust and erroneous attempt at segregation. Although no burden rested upon Appellees to do so, yet they voluntarily offered a segregation made upon just, reasonable, and practical bases in the District Court as between Texas and Oklahoma properties and operations which shows plainly that upon the basis of such segregation the order, as applied in Texas, is not confiscatory. Voluntary and unnecessary submission of such a segregation by Appellees, even if wholly unacceptable, did not lift from Appellant the burden of making a proper one:

Norfolk & Western Ry. Co. vs. North Carolina, 297 U. S. 682, 688-689, 80 L. Ed. 977;

Smith vs. Ill. Bell Tel. Co., 282 U. S. 133, 146-151, 75 L. Ed. 255;
Simpson vs. Shepard (Minnesota Rate Cases), 230 U. S. 352, 435-436, 461, 465-466, 57 L. Ed. 1511;
Great Northern Ry. Co. vs. Weeks, 297 U. S. 135, 143-145, 80 L. Ed. 532;
Smyth vs. Ames, 169 U. S. 466, 540-542, 42 L. Ed. 819, 847;
Wabash Valley Elec. Co. vs. Young, 287 U. S. 488, 497-498, 77 L. Ed. 447;
Houston vs. S. W. Bell Tel. Co., 259 U. S. 318, 322, 66 L. Ed. 961, 964;
United Fuel Gas Co. vs. R. R. Com. of Ky., 278 U. S. 300, 73 L. Ed. 390.

XXIII. Appellant was not in any event entitled to attack and strike down the order as being void *in toto*, and to prevent its operation as applied to the whole of Appellant's business and in all situations in Texas, even if (as is not admitted) under the Federal Commerce Clause the order could have been invalidated in part as applied to particular situations. The order is not indivisible or necessarily void as to all situations and business, even if shown to be void as to some, which latter we do not concede.

XXIV. Even if the order was, because of the claimed defense of interstate commerce, invalid in part as applied to particular portions of Appellant's property and business or as to particular situations (which is not conceded), the burden devolved upon Appellant (and was not discharged) of presenting clear, definite, and convincing evidence which would enable the reviewing courts to carve out such particular portions of Appellant's properties and business, and such particu-

lar situations, and to segregate same from the much greater properties and business, and the much more numerous particular situations, as to which the order was unquestionably valid and operative. If, for instance, the order was invalid as applied to the independent distributor at Gainesville (admittedly no interstate gas is served to the independent distributor at Waxahachie, R. V, 3006A, 3206A, I, 232-234, II, 1505) the attack should have been directed particularly at, and limited to, that particular situation; similarly, as to the towns where Appellant delivers at the city gates a mixture of gas from the Texas Panhandle, Oklahoma, and Central West Texas fields, Appellant should have directed its attack at, and limited it to, only that volume or portion of such gas at each particular city gate which came from a foreign state in interstate commerce and was, therefore, claimed to be exempt from state regulation; likewise, if the gas coming through Line A from the Panhandle field in Wheeler County, Texas, across the southwest corner of Oklahoma and back into Texas was gas moving in interstate commerce and, therefore, exempt from the regulatory control of Texas, as Appellant contends, before being commingled with Texas gas at various points in Texas, then the duty devolved upon Appellant to level its attack directly at, and limit it to, this particular volume of foreign gas at each city gate.

STATEMENT AND ARGUMENT UNDER POINT I

(Pp. 4-5, supra)

Throughout approximately seven months of hearings before the Commission, the Company deliberately and carefully abstained from every word and deed which would even suggest to the Commission any intention of the Company then, or later, to object that because of any claimed defense of interstate commerce the Commission was deprived of power to promulgate the order and make it applicable as it did. This fact is very plainly revealed by the statement of Appellant's counsel, (R. I, 305) that

> "It does not appear from the opinion and order of the Railroad Commission that the Commission would have found that 32c was a reasonable charge for gas moving throughout its entire transit up to the city gates in intrastate commerce, *had it been advised or had it known that it did not have the right to determine and enforce a rate applicable to all gas sold by the defendant.*"

This statement, it will be observed, was made not before the Commission, but in the District Court trial, *after* the Company had for the first time raised in its District Court pleadings (R. I, 124, 130, 136-137) the interstate commerce defense. Equivalent statements are made at R. II, 1496-1497.

The entire 11,232 pages of oral testimony adduced before the Commission, and all of the exhibits introduced before it, may be searched in vain for a single hint upon the Company's part to put the Commission upon guard that the Company intended then, or later, to raise any such objection. We have not seen fit to

incur an expense of $15,000.00 or $20,000.00 for having the Commission's record printed in this Court merely for the purpose of showing what it *does not* contain, but if the Company can point to anything in the Commission's record which would fairly put the Commission upon notice, or even upon reasonable suspicion, that the Company intended to raise any such objection or defense then or at any later stage, we will stand the expense of having such record excerpts printed as this Court may deem necessary.

This being true, we think the strongest possible case of estoppel is presented, to preclude the Company absolutely from attacking, or urging any defense against enforcement of, the order because of any claimed interstate commerce operations.

A defense of this character may be waived by the conduct, or silence and acquiescense, of the party litigant when under the duty to speak, the same as in the case of any other defense or ground of attack.

STATEMENT AND ARGUMENT UNDER POINT IV

(Pp. 7-8, supra)

See Commission findings, R. I, 25-28. Lone Star Gas Corporation owns in excess of 99 per cent of the voting stock of Lone Star Gas Company, (R. I, 235) and of the voting stock of every distributing company in Texas to whom Lone Star Gas Company sells gas, with the single exception of one independent distributor at Gainesville and one at Waxahachie, R. I, 235-237, 257. The volume of sales to the independent distributors at the two points mentioned are

relatively small; amounting to slightly over one per cent of total Texas deliveries, R. I, 297. Appellant and all of its affiliated companies maintain their general offices and places of business in two adjoining and interconnecting buildings in the city of Dallas, Texas, R. I, 237, 238, 250, 426-428. The completely interwoven and interlocking personnel and common members of the respective boards of directors and principal responsible officials of the various affiliated companies are shown in Chart R. III, 1917, 2175, and R. I, 235, 250, 314, 379-382, 238, 240-241, 245-246. Voting by proxy and power of attorney is done at stockholders and directors meetings, R. V, 3339, R. I, 249. Although Lone Star Gas Corporation has no permit to do business in Texas, (R. I, 235) it maintains in the Texas offices of its underlying affiliates a dummy or memorandum set of its books for the guidance and information of the affiliates, R. I, 428-429. Access to these Lone Star Gas Corporation books has always been denied the regulatory authorities of Texas, for the purpose of obtaining any information relative to the cost to the holding company of services claimed to have been rendered the affiliates by the holding company, or for any other purpose, R. III, 1880. The holding company habitually lends large sums of money to the underlying companies upon unsecured notes, at 6% annual interest, the money being advanced as and when needed. This indebtedness, in the case of Lone Star Gas Company, amounted to approximately $19,000,000.00 at its peak a few years before the hearing, but had been reduced to approximately $17,600,000.00 at the time of the hearing, R. I, 412. The unsecured advances to Community Natural Gas

Company amounted to $8,000,000.00 or $9,000,000.00, R. I, 242. All of the affiliated companies owed substantial unsecured amounts of money to the holding company with the possible exception of Municipal Gas Company, R. I, 243. Municipal Gas Company owed in excess of $100,000.00 to Lone Star Gas Company, unsecured, for city gate purchases, R. I, 245. Lone Star Gas Corporation is a Delaware corporation, with its nominal domicile in Wilmington, Delaware, but has its principal office at 800 Union Trust Building, Pittsburgh, Pennsylvania, R. I, 250. Lone Star Gas Corporation does most of its banking with the Union Trust Bank, of which bank G. W. Crawford, one of the principal stockholders, directors, and officials of the entire affiliated group, is also a director, R. I, 414, 472. The holding company is also a part owner of the Northern Natural Gas Company group, (R. III, 2058), consisting of 7 or 8 affiliated companies, of which D. A. Hulcy, one of the principal officials of the Lone Star group, is the common secretary-comptroller, R. I, 314.

The Lone Star group maintains common purchasing facilities in Pittsburgh, Pennsylvania, through the services of J. M. Simpson, Vice-president of Lone Star Gas Corporation, purchaser for the entire Lone Star group, and for the Columbia Gas and Electric Corporation group, a set-up controlling assets of about $600,000,000.00 to $700,000,000.00, R. I, 367, 417-418. The Lone Star group avails itself of the legal services of the General Counsel, who is a director, stockholder and official of various affiliated companies in the Lone Star group, in all rate litigation and other legal matters, R. I, 248. The Lone Star group also maintains a technical staff of rate litigation experts,

available to all companies in the group, consisting principally of the Company's principal witnesses in this cause, Hulcy, Biddison, Steinberger, and Connor.

The holding company has the right to select and control the selection of all members of the board of directors of each of the various affiliated companies in the group, and actually exercises such control, R. I, 377-378, 383-384. Hulcy testified in substance that he could not answer whether the directors of the underlying companies would be put off the boards if they failed to follow the wishes of the holding company, because such had never happened, R. I, 384.

In its attempt to justify payment of management fees to the holding company, the Appellant detailed much "advice" furnished it and the underlying companies, pertaining to all of Appellant's affairs, (but without even attempting to prove the cost to the holding company of such services); but to the discerning mind, the record reveals plainly that this is but an obvious camouflage of the absorption by the holding company of the profits of the Appellant, and that the "advice" would more appropriately be called "dictation" or "control" R. I, 239-244, 366-367, 411-413, 415-417, 419-420, 428-429, 434, R. III, 1640, 1880, 1902, 2126A. In addition to paying the holding company the management fees for such pretended "advice and services", Appellant also pays again for them, directly to the attorneys, engineers and auditors who furnish such "advice and services", R. I, 415-417.

Connor, (R. II, 1114-1115), for purposes of going concern value, considers the affiliates as being one integrated and commonly owned, controlled and op-

erated setup, from well to burner tip. But otherwise the Company insists they are all separate and independent entities.

If this record does not reflect a holding company which is not content merely to hold, we have never seen one.

In these circumstances we think there is not the slightest doubt that the highest state courts correctly disregarded the corporate fictions and treated the entire group as under a single ownership, management, and control, engaged in all three phases of the natural gas business in Texas.

STATEMENT AND ARGUMENT UNDER POINT VI

(Pp. 8-12, Supra)

The Company admits (R. I, 376) that it would not be practicable to segregate the properties, expenses, and revenues in such a way as to determine and fix a separate reasonable gate rate for application at each of the cities and towns, approximately 275 in number, served by its pipe line system in Texas. The Commission was thoroughly in accord with this view, and so are we. The only alternative was to fix a uniform gate rate for application at all Texas points upon the system. In order to accomplish its confessedly proper function of determining and fixing reasonable burner tip rates, the Commission had to pursue one of two methods: It could conduct 275 separate burner tip cases, and in each case hear full evidence upon the production and transmission phases (gate rate) and thus determine the reasonable cost of delivering gas to

the particular city gate; or it could in one hearing, fix a final uniform gate rate for the entire system in Texas, and later build the burner tip rates upon same after hearings as to the distribution operations only.

In view of the fact that the State has probably expended something in the neighborhood of $200,000.00 in the investigation, determination and defense of this 32c gate rate, and the Company has expended probably close to $1,000,000.00 in contesting the matter, the Court may gain some insight into the expense that would be involved in 275 repetitions of the gate rate case. And this is quite aside from the 6 years of time elapsed from the beginning of this proceeding to the present hearing.

We have stated frankly to the Court in Point VI the Commission's policy and intentions with respect to the treatment of the gate rate fixed in this proceeding. It is not a meaningless inquiry or quest after mere preliminary information, as this Court construed the gate rate inquiry and orders to be in *State Corporation Com. vs. Wichita Gas Company*, 290 U. S. 561, 78 L. Ed. 500, but is an indispensable step toward fixing ultimate burner tip rates, and is a final, binding and conclusive legislative act fixing the rate to be charged by the pipe line company and paid by the distributors for gas delivered at the city gates.

The Commission has expressly kept the proceeding open (R. I, 116) for further orders and modifications upon further appropriate application and proof by any interested party. That means that if, because of changed conditions or other reasons, the future should reveal that the 32c gate rate requires modification, the

Company or any other interested party may obtain it by due application and proof before the Commission in the gate rate cause, Gas Utilities Docket No. 75.

In all burner tip cases which have come before the Commission or the courts since the order, however, the Company has not chosen to so treat and accept the order as being final, binding, and conclusive upon the matters therein determined. In each of such burner tip cases the Company has insisted upon the privilege of introducing full evidence, and obtaining a complete *de novo* hearing, upon the entire production and transmission phases, as if the gate rate had never been heard or determined by the Commission. And this, notwithstanding the Company has never made application to the Commission in Gas Utilities Docket No. 75 for a modification of the gate rate fixed, but has chosen rather to defy and ignore it as a nullity and to attack it directly under the 14th Amendment in all the courts of the land, and to ignore and attack it collaterally in all burner tip cases based on the present order, both before the Commission and the reviewing courts. On the contrary, the Commission has insisted, and will continue to insist, both in fixing and defending burner tip rates in towns on Appellant's system, that the applicable gate rate has been finally and conclusively fixed by the present order, in Gas Utilities Docket No. 75.

Paradoxically, the Company has insisted that it is not permissible for the Commission to conduct any burner tip hearings, or enact any burner tip orders, or try any burner tip cases in the courts, until the final determination of this cause in this Court. If the Com-

pany's position be sustained, this Court can readily see what some of the consequent results would be. If the Commission had to suffer a period of six years to elapse from the initiation to the final determination of a gate rate, before even beginning the program of fixing burner tip rates based thereon, the process of rate making and ensuing litigation would be an endless one, and the entire program of rate regulation would be stymied pending perpetual litigation over the gate rate. If and when the Commission ever got around to the matter of fixing the 275 burner tip rates, each of these would require six years also to reach the stage of finality. Furthermore, the expense itself would be utterly prohibitive, considering that the gas consumers have to bear all the expense both on the State's and the Commission's side. This would result inevitably in a total break-down of the rate regulation program. And, doubtless, from the Company's standpoint that would be a "consummation devoutly to be desired."

Moreover, and more to the point, if the Company can defeat all state regulation merely by running one of its main transmission lines a few miles within Oklahoma, and by injecting a few atoms of Oklahoma gas into its 4,000 mile pipe line system, 86 per cent of which is located in Texas; and, retreating behind the bulwark of the federal commerce clause, establish that the state is entirely impotent to fix any gate rate at all, as the Company contends here, this would be even more effectively lethal to the state regulatory power than the Company's tactics above outlined.

Appellant relies especially upon *Missouri ex rel. Barrett vs. Kansas Natural Gas Company*, 265 U. S.

298, 68 L. Ed. 1027, and upon *State Tax Commission of Mississippi vs. Interstate Natural Gas Company*, 284 U. S. 41, 76 L. Ed. 156, as establishing that the Commission has not the power to do that which it has undertaken to do in this case. Both of those cases are plainly and readily distinguishable from this case upon several different grounds, the most obvious of which is that in those cases the whole volume of gas was transported from another state; the sales involved in those two cases were being made only at wholesale by an interstate transporter of gas to *independent and non-affiliated* distributing companies, and not to *alter egos* or affiliates owned, operated and controlled by the transporter or by a common holding company who owned and operated and controlled both the transporter and the distributor as is the case here; and further, the transporter was not there shown to be engaged in the numerous and extensive intrastate distribution and other activities that Appellant carries on in Texas, nor had the gas been subjected to the numerous methods of treatment and inextricable commingling shown here, which would deprive it of any interstate character it may ever have possessed.

Appellant has seemed especially to rely upon this Court's language in the *Barrett case* that "The paramount interest is not local but national,—admitting of and requiring uniformity of regulation. Such uniformity, even though it be the uniformity of governmental non-action, may be highly necessary to preserve equality of opportunity and treatment among the various communities and states concerned." That language, regardless of how appropriate it may have been to the

particular case there under consideration, can have no application to the situation here. In the first place, it is addressed to a question of legislative policy and not to a justiciable question of law or fact. *South Carolina State Highway Commission vs. Barnwell Bros.*, ——————U. S. ——————, 82 L. Ed.——————. In the second place, the State of Oklahoma and its communities can have no possible interest in what rates may be fixed by the State of Texas for the sale and distribution of gas in local commerce within the State of Texas. Likewise, Oklahoma can have no interest in what gate rate may be applied in Texas as a basis upon which to build local Texas burner tip rates.

Appellant's contention in this respect boils down to an insistence (R. V, 3500-3501) that although the state may admittedly, for all practical purposes, fix the rate to be *charged* by the Appellant and directly fix outright the amount which may be *paid to* Appellant by the distributors, at all city gates in Texas, even for interstate gas, by the indirect method of fixing in burner tip cases "what such companies may reasonably *pay and charge* for the gas sold to them by the defendant at the city gates," that it cannot accomplish the same result directly in a uniform gate rate case by ordering the affiliated pipe line company not to *charge and receive from* the distributors in excess of a certain sum. We submit that this is a distinction without a practical difference. The ultimate effect upon interstate commerce in either instance is identically the same.

Where the distributors and the pipe line company are affiliated with and controlled by, a common parent holding company, as is the case here, the situation

amounts to no more than this: That the entire system and operations from well to burner tip are owned, managed, and controlled by a single corporation, and the Commission has in this order merely fixed the price to be charged by that corporation—not upon a sale to someone else, for there is no sale possible from oneself to oneself—but a price to be set up as a reasonable charge for all operations by that single corporation up to and including deliveries at the city gates. *State of Texas vs. Public Service Corporation of Texas,* 88 S. W. (2d) 627, writ refused. In such case the money all goes into and comes out of a common pocket in any event—that of the holding company—and it makes no difference how the ultimate process of local burner tip regulation be accomplished—whether step by step or all at one fell swoop; whether directly or indirectly. In the case of sales to a non-affiliated distributor the fixing of a maximum operating expense which the distributor may set up for gas purchases at the city gate is equally effective for all practical purposes in determining the amount realized at the city gates for interstate importations of gas, because the independent distributor, in its desire to avoid certain and immediate financial bankruptcy, would be impelled by motives of self-preservation not to pay more to the independent pipe line company than it would be allowed to cover into its burner tip rates. In the present case there are involved sales of only relatively small volumes (R. I, 297) to only two independent distributing companies. Admittedly no gas claimed by the company to be transported in interstate commerce is delivered at the city gate of Waxahachie, R. II, 1505, R. I, 232-234; Map R. V, 3006-A,

The small volumes of sales to the independent distributing company at Gainesville are the only ones in which the interstate commerce question could have any possible application as to an independent distributing company.

Appellant cites only one case by this Court on the question of a state's power to fix a gate rate on interstate gas transported and sold to it *affiliates* in the receiving state. That was only a *dictum*, in *State Corpn. Commission vs. Wichita Gas Co.*, 290 U. S. 561, 563-564, 78 L. Ed. 500, 502. The statement is expressly admitted to be only dictum, (290 U. S. 568) where this Court states that it is unnecessary to pass upon the validity of the gate rate orders, there involved. None of the four cases cited supports the dictum.

STATEMENT AND ARGUMENT UNDER POINT VII

(Pp. 12-13, supra)

If the State appellate courts were correct (as we believe unquestionably they were) in holding that because of common ownership, operation, management, and control of all natural gas operations the Lone Star group of affiliated companies is to be considered in legal contemplation as a single unified owner, then in reality there are no sales at any city gate in Texas, where the interstate commerce question would have any possible application at all, with the single exception of the small volumes sold to the independent distributor at Gainesville, R. I, 257.

This being true, aside from said small sales to the Gainesville Gas & Electric Company there is no "commerce" carried on in the State of Texas by the Appellant or its affiliated group of companies save and

except the admitted intrastate commerce of sale and distribution of gas direct to its local consumers in Texas, and the sale of admittedly intrastate (West Texas) gas to Waxahachie Gas Company at the city gate of Waxahachie.

STATEMENT AND ARGUMENT UNDER POINT VIII

(P. 13, supra)

None of the cases cited by Appellant on page 65 of its brief is in point upon the operations here involved.

Hanley vs. K. C. S. Ry. Co., 187 U. S. 617, 65 L. Ed. 104, and *M. P. R. Co. vs. Stroud*, 267 U. S. 404, 69 L. Ed. 683, involved interstate carriage of freight, by common railroad carriers, between termini in the state of origin and destination, but over a route crossing state lines; which field of regulation had been expressly taken over and removed from the field of permissible state regulation by the terms of the interstate commerce act, which had the effect of broadening the scope of regulation beyond what otherwise would have been held to be interstate commerce, *per se*, immune from state regulation, in the absence of such a national statute.

State Tax Com. vs. Interstate Natural Gas Co., 284 U. S. 41, 76 L. Ed. 156, involved sales of gas by an interstate transporter to independent distributing companies at wholesale, the entire volumes having been imported from another state.

Western Union Telegraph Co. vs. Speight, 254 U. S. 17, 65 L. Ed. 104, was decided by this Court virtually by default, no brief or argument having been

submitted on behalf of the respondent. The terse opinion by Mr. Justice Holmes cites only *Hanley vs. K.C.S. Ry. Co. supra*, and *Kirmeyer vs. Kansas*, 236 U. S. 568, the latter a liquor case; and neither case is in point. The Court properly decided this question in *Lehigh Valley Ry. Co. vs. Pennsylvania*, 145 U. S. 192, 201-202, 36 L. Ed. 672, and the other cases cited by us under our Point VIII.

STATEMENT AND ARGUMENT UNDER POINT IX

(Pp. 14-15, supra)

A mere glance at the map of Line A, in the appendix to Appellant's brief, should be almost sufficient to convince the Court that the Company could have no purpose in detouring and extending that line a short distance within and parallel to the Western boundary line of Oklahoma, except to attempt evasion of state regulation. See Company map, R. V, 3009-3010, showing that there are no gas fields in Oklahoma within reach of Line A, and also that on the Texas side the terrain is smooth, level and free of obstructions, whereas the actual route of Line A in Oklahoma crosses many streams and much rough country.

Many other pertinent facts are reflected by the record, however, to reinforce that conclusion. The Commission's witness Freese testified (R. I, 269-272) that *Line A* could have been constructed as cheaply wholly within Texas as over the route chosen; that a smaller quantity of rock excavation would have been encountered; that the line would have been laid on a straight course instead of a curve; and would have been ap-

proximately five miles shorter than the existing line; and furthermore that it could have been routed through Wellington, a town of 1,968 population (not now served by the line) instead of Hollis, Oklahoma, with a population of 1,699, which is the only Oklahoma town served by Line A on the section within Oklahoma, and which town could as well be served by a slightly longer tap line from the main line wholly within Texas. The Commission's witness French had personally inspected the parallel transmission line of Northern Texas Utility Company, constructed at about the same time as, or later than, *Line A*, wholly within Texas, from the Texas Panhandle Field to the City of Wichita Falls, Texas, and intervening points; he testified that he made excavations and classified the soils on this line and checked them against the original field construction notes of the line; that on this line he classified 91.94 per cent as machine excavation, 1.53 per cent as loose rock, .45 per cent as solid rock, and 6.08 per cent as hand earth excavation; that he found no unusual difficulties on the Texas route; that the river crossings on the Texas route were not unusually difficult or expensive to construct, R. III, 1843-1851. Contrast Steinberger's classification (R. II, 1253) on that portion of Line A in Oklahoma only, as machine excavation 86.5, hand earth 5.3%, and rock 8.2%.

STATEMENT AND ARGUMENT UNDER POINTS X, XI, XII, and XIII

(Pp. 15, 16, 17, supra)

Prior to 1918, the tremendous natural gas deposits in Texas had not been discovered or developed. The

only extensive Texas field developed prior to that was the Petrolia Field. Upon incorporation of Lone Star Gas Company in 1909, certain leases in that field owned or controlled by the incorporators were transferred to Appellant in payment of a substantial amount of its original $2,500,000 capital stock, R. III, 1879. Its original line supplied gas only to Fort Worth and Dallas, Texas, and intermediate towns between those points and the Petrolia Field. About the year 1918, with the discovery of the Ranger Field in central west Texas extensive reserves were developed in that area and tapped by extensions of Appellant's system. In 1918, Appellant constructed Line G from the Fox, Loco, Palacine and other fields in Oklahoma. In 1918 Line H from Walters, Oklahoma, to Petrolia, Texas, was completed and joined with Appellant's system. In 1919, Line Second H, Walters, Oklahoma to Petrolia, Texas, was completed and connected with the system. In 1926-1927, Line A from the Panhandle Field in Wheeler County, Texas, to Petrolia, Texas, was constructed and connected, R. I, 368.

At the time of the trial, therefore, the Company was obtaining its supplies from three principal sources —Central West Texas Field from which the gas was transported eastward; the Texas Panhandle Field, in Wheeler County, from which it was transported south-eastward, through Line A; and the Oklahoma Fields, from whence it was transported southward, through Lines G, H, and Second H. According to the Company's computations at page 28 of its brief, it is deducible that the following percentages of Appellant's total deliveries in Texas and Oklahoma were ob-

tained for the following years from the three principal sources:

Year	From West Texas Fields	From Panhandle Fields	From Oklahoma Fields
1929	67.1 per cent	14.8 per cent	18.1 per cent
1930	69.3 per cent	16.5 per cent	14.2 per cent
1931	74.0 per cent	17.0 per cent	9.0 per cent
1932	70.4 per cent	23.3 per cent	6.3 per cent
1933	76.7 per cent	19.5 per cent	3.8 per cent

State's Exhibit No. 5 (R. I, 297) shows that Oklahoma produced gas, for the following years, constituted the following percentages of Appellant's total deliveries in Texas:

1931	10 per cent
1932	7 per cent
1933	4.5 per cent

As offsets against these quantities of Oklahoma gas consumed in Texas, it should be remembered that there were very large, rapidly and constantly increasing volumes of Texas gas being consumed in Oklahoma. Company witness Schmidt testified that if the past rate of decline in Texas consumption of Oklahoma gas from 1929 to 1933, inclusive, should continue there would be no Oklahoma gas consumed in Texas by the end of 1934, R. II, 1481, 1482-1487.

In the District Court trial, Company Witness Connor testified that the Company intended to take up and remove Line H, (from Oklahoma) during the year 1934, R. II, 1417. This line has now actually been removed in accordance with the Company's in-

tentions thus expressed; leaving only Line G and Line Second H to bring gas to Texas from Oklahoma. The system map (Appendix to Appellant's brief and record V. 3006A) show three main transmission lines extending from Petrolia, Texas, to the vicinity of Dallas and Fort Worth, Texas. These are lines B, Second B and the "Government 10-inch Line" (the last-named line being excluded from the appraisal and being the line used in carrying out Appellant's contract with the U. S. Government for supplying its helium plant from whence the helium contract revenues were derived which are segregated in the Commission's opinion, R. I, 20.) Line Second B has also now been taken up and removed.

Commission's Exhibit No. 4 (R. III, 2124 A) closely compared with Commission's Exhibit 5 (R. III, 2126 B) shows that after offsetting the deliveries of Texas gas as against Oklahoma gas delivered in Texas, there is a net balance in the exchange, favorable to Oklahoma, of the following percentages of the Company's total deliveries in both states:

Year	From Oklahoma Fields
1929	16.9 per cent
1930	13.0 per cent
1931	6.7 per cent
1932	4.2 per cent
1933	.4 per cent

The obvious reason for the continued sharp and steady decline of Texas importations of Oklahoma gas are the depletions and failure of the older Okla-

homa Fields and the simultaneous discovery and opening of the vast new fields in Texas. The Company's Line A now taps the Shamrock Field in Wheeler County, Texas, and in addition, its own evidence shows that it owns or controls vast undeveloped deposits in Gray and Carson Counties, Texas, west of Wheeler County, all being parts of the vast Texas Panhandle Field of the extent of which this Court took judicial notice in the recent case of *Thompson vs. Consolidated Gas Utilities Corporation*, 300 U. S. 55, 81 L. Ed. 510. The Company witness, Schmidt, recognizes (R. I, 222) that this is one of the largest gas reserves in the world.

The Company also admits that it possesses other vast developed and undeveloped gas reserves in the West Texas fields; and in the past it has produced from its reserves only about 20 per cent of its total deliveries, and has purchased the remaining gas, approximately 80 per cent of its deliveries. The prevailing wellhead price in the Texas Panhandle Field, observed by the Company since 1926, has been 2c per M C F, R. I, 581. In the West Texas Fields the prevailing price is approximately 6c per MCF R. I, 586. In Oklahoma the prevailing wellhead prices are as follows: Chickasha, 8c; Duncan, 10c; Loco, 6c; R. I, 593-594. The Company formerly purchased gas from its affiliate, Meridian Gas Company in the Chickasha, Oklahoma, Field, at 15c per M C F, R. I, 108. The average overall field prices paid by the Company in Texas and including much more expensive Oklahoma purchases, from 1920 to 1933, are shown at R. I, 606-607.

Appellant will not deny that since the close of the District Court record it has removed lines H and Second B, and has constructed two large transmission mains from the Long Lake and Cayuga fields in East Texas to points near Dallas and Waco, Texas, respectively, where said transmission lines connect with Appellant's pipe line system.

Dunn testified that the Company owned in total semi-developed and marketable gas reserves in proven areas, 367,362,084,000 cubic feet. R. I, 524, 525, 535.

Dunn further testified that the Company had in the semi-developed reserves a forty year supply based upon the 1933 production; testifying that in 1933 the Company produced from 7,000,000 to 9,000,000 M C F, R. I, 534.

Hulcy testified that if the withdrawals were 9,000,000 or 10,000,000 MCF a year, there was not any question but that it would be sufficient to last approximately forty years. R. I, 577.

It should be noted that the witnesses testified that the Company-produced gas was approximately 9,000,000 MCF for the year 1933. They did not point out, however, that this 9,000,000 MCF was considerably in excess of the actual withdrawals during that year from the Company's reserves, or that it included the volumes of inert gas introduced into the West Texas gas at the Joshua dilution plant just southwest of Fort Worth, Texas, R. II, 1571. The actual withdrawals from the Company reserves for

the years 1927 to 1932, inclusive, were as follows: R. I, 107.

1927	2,671,443 M Cubic Feet
1928	3,451,935 M Cubic Feet
1929	5,162,647 M Cubic Feet
1930	6,473,463 M Cubic Feet
1931	4,924,844 M Cubic Feet
1932	4,829,077 M Cubic Feet

The withdrawals from Company-owned reserves for 1933 were 6,046,035 M Cubic Feet, being 5,432,255 M cubic feet from Texas reserves, and 613,780 M cubic feet from Oklahoma reserves. R. III, 2165, 2124A.

Based upon actual withdrawals from the Company reserves for 1933, which are 6,000,000 MCF, it can readily be seen that the Company has a sufficient volume in its developed marketable reserves to last sixty years. Company Exhibit 30 (R. V, 3019), shows that by volume the Company's developed marketable reserves in Oklahoma are only 1.2% of those in Texas. Hulcy (R. I, 458-459) admits that 95% of the Company's entire business is in Texas against 5% in Oklahoma; while 13.8% of its pipe line mileage is in Oklahoma and the remainder in Texas.

These facts, and others appearing in the record, suffice to show clearly four things:

(1) That during and since 1933 there has been no necessity or occasion for the Company's importing a single cubic foot of gas from Oklahoma, or any other state, to meet the Company's Texas demands.

(2). That the Company's developed marketable reserves, aside from its undeveloped reserves and its unlimited purchase contracts and connections in Texas, are more than sufficient to meet its entire probable Texas demands for a period of many years in the future, and that this has been the situation for at least several years in the past.

(3) That instead of there being a net flow of gas from Oklahoma to Texas during and since 1934, there is in all probability now, and has been since 1934, and will continue to be in the future, a greater and increasing flow of Texas gas to Oklahoma than of Oklahoma gas into Texas. Company witness Schmidt himself testified (R. I, 225-226) that the gas at various times flowed in both directions in line G. Hulcy testified the same as to the whole system, R. I, 376. At Record I, 229, Schmidt attempted to modify his testimony in that respect, but still admitted that this occasionally happens. At R. II, 1470-1471, he finally denied belief that it has happened.

(4) That both because of the higher prevailing wellhead prices on gas purchased in Oklahoma, and because of the Company's greater investment per meter in Oklahoma than in Texas, the Company's operations in Oklahoma are very much more expensive and less profitable than those in Texas. The Company so admits, R. III, 1594.

STATEMENT AND ARGUMENT UNDER POINT XV

(Pp. 18-20, supra)

Under the Commission's order the Company is left free, as it has always been, to import as much gas into

Texas, and to export as much gas from Texas, as it pleases, and to permit a free interflow of gas from any and all sources within its lines as it may see fit. There is absolutely no prohibition, restriction, impediment or burden upon the free interstate flow of gas. The only effect of the order is that from whatever source the gas comes to the city gates in Texas it must all be sold at a reasonable price, including foreign and Texas gas alike. The effect of such an order upon interstate commerce, if any interstate commerce be involved at all, which we deny, is certainly not a direct and substantial burden upon the same, but is at most only an incidental, indirect, remote, unsubstantial and unprohibited burden. The order is made applicable in Texas only: R. I, 15.

STATEMENT AND ARGUMENT UNDER POINT XVI

(Pp. 20-21, supra)

The record shows that when the gas leaves the Texas Panhandle field through Line A, and the Oklahoma fields through lines G and Second H (line H having now been removed) the Company does not know what the ultimate destination of the gas is. It is not destined for any particular locality, but is only started off in a general direction destined for general commingling in the northern part of the system, R. I, 225-226, 376. No sales are made of the gas, or of any particular volume thereof, to any person prior to the time it arrives in Texas; and our view is that (corporate fictions disregarded) no sale is made of it to any person after its arrival in Texas, except to the ultimate consumers at the burner tips—with the single exception of the small sales to the independent distributors

at Gainesville and Waxahachie. The gas simply flows along its way until by fortuitous circumstance of load demand it is drawn out of the line.

Schmidt testified the direction of flow in Line G alternates (R. I, 225-226) and Hulcy says the same of the whole system. R. I, 376. Dunn testified (R. I, 531, 224) that he is the sole person who determines where the supply of gas shall be withdrawn or purchased, and where it shall be directed to in the 4,000 mile system of the Company. In these circumstances it will readily be seen that it lies easily within the power of the Company to shift its withdrawals and transportation from day to day, and from hour to hour, and from year to year, in such way as totally to evade and defeat effectual regulation by any and all state authorities and even by federal authority, if a federal regulatory body should be provided by Congress. See how the proportions of gas from the various sources may be shifted at any given point by the Company from day to day, R. V, 3241. When a proceeding should arise before any state body the Company would merely have to transport a little gas into its system from Oklahoma, and under its theory the entire operations would be exempt from state control in both states as interstate commerce. On the other hand if an inquiry should arise before a federal regulatory body next day, all the Company would have to do would be to shut off the supply of gas from Oklahoma and there would be no interstate commerce involved. The only practicable way in which any effective regulation can be provided at the present time in Texas is to uphold the Commission's right to regulate in the manner in which it has been done here.

STATEMENT AND ARGUMENT UNDER POINT XVII

(Pp. 21-23, supra)

The gas coming through Line A is run through a gasoline extraction plant at Hollis, Oklahoma. Schmidt describes the process. Similar treatment is given the gas coming through Lines H and Second H at the gasoline plant in Petrolia, Texas, and Line G at the gasoline plant at Gainesville, Texas. Schmidt testifies (R. II, 1479) that the extraction of these volatiles reduces by about 3% the BTU heating content of the gas. He also says (R. II, 1484) that in this extraction process the gas is allowed to expand somewhat from its higher pressures in a 30" diameter tank and filter through an extraction oil. He admits (R. II, 1591) that the extraction process changes the B. T. U. content of the gas. Schmidt pretends that the gasoline is extracted only to prevent line trouble, (R. II, 1479, Brief p. 32) but he admits the Company has made profits on the gasoline; and the Company repressures the gas into the "Miller Farm" near Petrolia, Texas, to absorb more gasoline and recover and extract same for profit, R. II, 1484.

Appellant, at p. 24 of its brief, quotes a provision said to be inserted in its gate rate contracts to the effect that the distributing companies shall install and operate "such regulators and regulator stations as it may require to regulate the pressure of the gas *after delivery thereof by vendor to vendee.*" The statement is ambiguous, and even misleading, unless one knows the significance of the language we have put in italics. The actual facts are that although the gas arrives at the city gate measuring stations at pressures ranging

from 100 to 350 pounds per square inch. Appellant itself owns, maintains and operates the first regulator or reducing mechanism through which the pressure is reduced to 25 or 30 pounds at the outlet side of the regulator before being metered and delivered to the distributors. At the next stage after this pressure reduction, the gas goes through the meter and is there measured and delivered to the distributors under this reduced pressure.

An examination of the Company's appraisal, Exhibit 28, will show that Appellant owns both the regulators and meters through which the gas is passed before delivery to the distributors. An example will be found at R. IV, 2386, and many others may be found in the record. The Company's witness Schmidt testified specifically (R. II, 1469-1470) that title to the gas does not pass to the distributors until it passes through the reducing regulator and is metered at low pressure and reaches the outlet side of the meter. At brief, p. 25, the Company states that this reduction in pressure "is done to accommodate the distribution plants in their operations" and solely for that purpose. It will be observed, however, that in the gate rate contracts the Company is specifically obligated thus to reduce the pressures before deliveries, a good example being found in the contract with the independent distributor Gainesville Gas & Electric Company (R. IV, 2325), requiring the Company to reduce the pressure to 20 pounds per square inch. For a similar provision in the contract between Lone Star Gas Company and Municipal Gas Company see R. IV, 2319. See also R. I, 219; R. II, 1470. Thus it will be seen that what the contract provision means, as quoted by the Com-

pany on page 24 of its brief, is that the distributing company shall install and operate only "such regulators and regulator stations" as the distributors may require to *further* reduce the pressures from 25 or 30 pounds to 4 or 6 ounces, after delivery to them, and before delivery to the retail domestic consumers. This shows clearly, also that the Company makes a gross mis-statement when, at p. 106 of its brief, it says, "There is no evidence of any reduction in pressure except that effected by the regulators of the distributing companies."

It is shown further that Appellant operates the retail distribution system in the important city of Fort Worth (shown in the exhibits and testimony as "Lone Star Gas Company, Fort Worth Division") where the local service necessitates that the gas be reduced to pressures as low as 4 to 6 ounces before delivery to the customers, and where approximately 33,000 customers are served (R. I, 219, 328; R. III, 1896).

The same situation prevails, as reflected by the Company's exhibits and testimony as well as those of the Commission, as to the retail domestic, commercial and industrial sales made by the Company on its rights of way over its entire system. In these cases the Company owns, maintains and operates the regulator equipment and the meter equipment. See for instance the item of gas connections $15,050.78 (R. I, 339), and also Company's Exhibit 5, R. III, 2211. For sales at farm taps on main lines see R. I, 407. For field and miscellaneous sales in Texas operations see R. III, 1641, 2116B. For list of numerous large industrial and commercial concerns served

directly by Appellant in Texas, see the following references: R. IV, 2393, 2406, 2407, 2409, 2414, 2415, 2428-2430, 2435, 2438, 2440, 2447, 2452, 2453, 2457-2459, 2464-2466, 2476-2477, 2492-2508, 2520-2522, 2525, 2535-2543, 2547-2556, 2558, 2560-2564, 2566-2589; R. III, 1693-1695.

A mere examination of the various system maps in the record, and the evidence generally, will disclose the even in the Company's transmission system, through its tap and lateral lines to retail domestic, commercial and industrial customers on its rights of way and in its tap lines to the city gates, the high pressure streams of gas in the main lines are broken up into much more numerous and minute streams.

See also the important industrial sales to West Texas Utilities Company, R. III, 1693-1695, shown by the map appendix to Appellant's brief, near the southwest corner of Oklahoma, as having been 1,713,055 MCF for 1933, out of a total production for that year from the Texas Shamrock Field of 6,448,138 MCF. The drawing off of this great quantity at that point to a single industrial customer in Texas necessarily "breaks the original package" even if the Line A gas be considered originally interstate gas. It will be seen that this is the first tap in Texas, as shown in map in Appellant's brief, and this takes place before any deliveries are made at any city gates; at each of which gates a further "breaking" takes place, of course.

Near Petrolia, in Texas, is located what is referred to in the record as the "Miller Farm," a depleted gas lease in which the Company for several years has been

repressuring or storing gas derived in part from Line A, (R. II, 1478, 1541), but mostly from Lines H and Second H coming from Oklahoma. The gas is there stored ordinarily in the summer time and withdrawn during the winter. The volumes so repressured or stored, in excess of the amounts withdrawn, are shown in Appellees' Exhibit 4, R. III, 2124-A. Since this table shows only the excess of volumes stored, over volumes withdrawn, the actual volumes stored greatly exceed the volumes shown by the table. Schmidt testified that 500,000,000 cubic feet were stored in this farm in 1933 alone, R.II, 1486-1487; R.I, 593; R.II, 1484-1485. It is obvious that gas stored in these sands is totally arrested in its movement for periods of six months or longer; nevertheless, Company witness Schmidt denies such fact, and states that it just "circulates through the sand", R. II, 1483. Schmidt's idea, thus expressed, as to what constitutes an "arrest" of movement of gas may explain his testimony, R. II, 1478-1484, that the forward movement of the gas is not arrested when it passes through the expansion tanks of seal oil in the gasoline extraction process.

In view of the decisions of this Court, cited under Point XVII, we believe it plain that the Company's entire business in Texas is intrastate, and subject to regulation by the Commission.

STATEMENT AND ARGUMENT UNDER POINT XIX

(Pp. 26-27, supra)

Statements and Arguments under Point XVII are adopted.

The record shows that in addition to the numerous other intrastate activities engaged in by the Company in Texas, and hereinbefore pointed out, the Company and all of its affiliates maintain their general offices in Dallas, Texas, where the entire business of said companies is transacted and carried on, R. I, 426-428, 237-238. We believe this brings the case squarely within the decision of this Court in *Southern Natural Gas Corporation vs. Alabama*, 301 U. S. 148, 81 L. Ed. 970, affirming *Alabama vs. Southern Natural Gas Corporation*, 170 S. 178.

STATEMENT AND ARGUMENT UNDER POINTS XX TO XXIV, INCLUSIVE

(Pp. 27-31, supra)

As shown under Point I, supra, Appellant did not raise the defense of interstate commerce before the Commission, nor was any segregation of any character made before the Commission in the evidence of either party. As a consequence the Commission received evidence from both parties as to overall property valuation and operations of the Company in both Texas and Oklahoma.

The evidence before the Commission, and District Court alike, discloses that because of the relative scarcity of gas in Oklahoma, and the consequent higher wellhead prices there prevailing, ranging from 6c to 15c per MCF, paid by the Company for gas purchased in Oklahoma, (R. I, 593-594, 108), and because the Company's investment per meter in Oklahoma was much higher than in Texas, the intrastate operations

in Oklahoma were very much more expensive and less profitable to the Company than those in Texas, R. III, 1594. This situation was not brought about by the State of Texas, the Commission or the consumers in Texas, but was a natural advantage bestowed by nature herself. This being true, we do not conceive that the consumers in Oklahoma, whose rates are to be fixed by the Corporation Commission of Oklahoma, are entitled as a legal or moral right to the same rates for natural gas as are the consumers in Texas.

Nevertheless, the Commission was fully cognizant of that situation, and took special note thereof, (R. I, 107-108) in pointing out the higher wellhead prices paid in Oklahoma; and also (R. I, 15) in stating that "the Company's Texas properties and its Oklahoma properties constitute parts of an integrated operating system. For that reason, *we have considered the Oklahoma properties and operations and the effect thereof on the revenues and the expenditures within Texas.*" The Commission realized, of course, that it had no jurisdiction to fix rates applicable in Oklahoma, so it continued: "On this basis we have fixed a rate for application *within the jurisdiction of Texas.*"

These markedly less profitable operations in Oklahoma were brought more sharply to the fore in the segregation made by Appellees before the District Court. The exhibits and testimony of Appellee's witness Phillips (R. III, 1667-1668, 2116-A, 2126-A) show that the net earnings, before providing for de-

preciation and depletion, attributable respectively to the Oklahoma and Texas operations, were as follows:

1931 - Texas	$4,758,714.46	= 96.9%
1931 - Oklahoma	150,456.67	= 3.1%
1932 - Texas	4,882,297.56	= 97.4%
1932 - Oklahoma	128,178.93	= 2.6%
1933 - Texas	4,185,327.48	
1933 - Oklahoma, a loss of	61,531.12	(red)

Year ending March 31, 1934, (overlapping nine months with 1933):

Texas	$4,416,571.74	
Oklahoma, a loss of	30,277.50	(red)

. The properties are 86% in Texas and 14% in Oklahoma, R. III, 1736-1737, 2142, 2157.

Although this great disparity in profit between Oklahoma and Texas operations was perfectly apparent to the Commission, it deliberately favored the Company, and the Oklahoma consumers, by fixing its rate at such a figure as that, if applied overall to the Company's entire operations in both Texas and Oklahoma, it would yield a reasonable net average return of 6%.

Totally ungrateful for this generosity, the Company immediately attempted to stab the Commission in the back by raising for the first time in the District Court the claimed defense of interstate commerce.

This new attitude upon the Company's part imposed upon it the burden of making before the District Court a segregation, first, as between its admittedly intrastate operations and the operations which it claimed were exempt from state control as inter-

state commerce, if it wished to sustain such defense; and, secondly, it thoroughly justified Appellees in insisting also that, if such a defense were to be interposed, there should be made also a segregation between Texas and Oklahoma properties and operations, so as to exclude the less profitable (and, for 1933, losing) Oklahoma business (R. III, 1594; 2116A, 2126A, 1667-1668) from consideration in determining whether the rate as applied only within Texas was unreasonable, unjust or confiscatory.

From the beginning of the District Court trial, however, until practically its close, the Company insisted that no segregation upon either basis was necessary or permissible, but that it was entitled to attack the order upon the same overall basis in Texas and Oklahoma as the Commission had used in fixing the rate. Appellees were firm in their insistence, however, that segregations should be made by the Company upon both bases, as part of the burden of proof devolving upon the Company, if in fact there were any interstate commerce involved.

The Company apparently was not very confident of its position, however; and finally yielded to the insistence of Appellees, to the extent of submitting a purported segregation as between what it chose to call "interstate and intrastate operations." R. II, 1500. The Company insisted that if any segregation were necessary or proper at all, the burden was upon the state, and not upon the Company, to make it, R. II, 1496-1497; also see R. I, 325-327, 376, 392-393, 482, 558, 568; R. III, 1629, 1735; R. II, 1142-1143, 1230, 1235, 1264.

The Company admitted that its records were kep in such way as to permit of easy segregation betwee Texas and Oklahoma properties and operations R. I, 390-393, 456-460, 481-482, 508, 557-558 570; R. II, 1143.

The Company also insisted that no segregation wa necessary or permissible in the District Court, becaus the Commission had made none. This contention i refuted by this Court's decisions in *Smith vs. Illinoi Bell Telephone Company*, 282 U. S. 133, 75 L. Ed 255, where the Illinois Commission had made no seg regation whatever between intrastate and interstate op erations in fixing local telephone rates for Chicago and where this Court remanded the cause, not to th Commission for further findings and segregation, bu to the *District Court* to make a proper segregation and where, after the segregation had been made by the District Court, and findings made by it holding the rate confiscatory upon the basis of such segregation this Court reversed the second District Court judg ment and finally upheld the rate as non-confiscatory *Lindheimer vs. Illinois Bell Telephone Company* 292 U. S. 151, 78 L. Ed. 1182.

The Company did not purport to make any segre gation whatever in the District Court as betwee Texas and Oklahoma properties and operations. Th segregation which it did make purported to be one be tween what Hulcy thought were "interstate and in trastate" operations; (R. III, 1604) and was worke out and sponsored by Schmidt, Connor, and Hulcy The first step was Company's Exhibit 45 (R. V 3207) which was a purported segregation only of th

gas supposed to have been produced in the Wheeler County, Texas, field and the Oklahoma fields on the one hand, and the West Texas gas on the other hand; and this segregation is based upon the specific gravity tests hereinafter discussed. The remainder of the segregation was made by Hulcy in Company's Exhibit 46 (R. V, 3279) which exhibit relates to properties, revenues and expenses.

Schmidt, in Company's Exhibit 45, provided the sinking-sand foundation upon which was constructed the Company's segregation of properties, revenues and expenses as between what the Company asserts as interstate and intrastate operations. It is in no sense a segregation as between Texas and Oklahoma property, revenues and expenses. The segregation is based upon the determination of "specific gravity" of gas in the Company's lines at some 11 or 12 points where it kept apparatus for such determinations. The Company made such a segregation based upon specific gravity determinations for the year 1933 only, which year admittedly was an abnormally warm year, R. III, 1594-1595. Even if the segregation were otherwise acceptable, being for 1933 only, it is too short a spread of experience on which to base a rate. Schmidt testified that Oklahoma-produced gas had a specific gravity of about .63. He also testified the specific gravity of the gas from the Panhandle area of Texas was about the same, R. II, 1499. The specific gravity of the gas from Central West Texas averages .785 to .83, R. II, 1499-1500. He left out of account the gas from Petrolia field, whose BTU content and specific gravity were different from all of the other gas. See also R. II, 1568-1569, showing that the West Texas gas had a

higher BTU content (1200) until it was diluted with inert gases at Joshua. Also R. II, 1591, giving BTU content of Texas and Oklahoma gases. He further testified that, based upon his specific gravity determinations, a segregation of Oklahoma gas could not be made from that gas produced in the Texas Panhandle, at any particular point on the system, R. II, 1579. This being true it was impossible to segregate the Texas Panhandle gas on the one hand from the Oklahoma-produced gas on the other hand at any given point on the system; therefore, he would be unable to determine by this test the combined volume of West Texas gas and Texas Panhandle gas as distinguished from the volume of Oklahoma-produced gas at any particular point in the system.

Schmidt testified that in the preparation of Exhibit 45, it was necessary to take into consideration the specific gravity of the gas, the pressure base, the temperature of the gas, and the barometric pressure at the point of measurement, (R. II, 1499); that the specific gravity will make a difference in the volume in the relation of the "inverse portion" of the square root of the gravity; that the specific gravity of the gas produced and transported from the Central West Texas area ranges in specific gravity from about .785 to about .83. (R. II, 1699); that the BTU content of the gas is changed after passing through gasoline plants (R. III, 1591); that the Oklahoma gas from line H and second H goes through a gasoline plant. (R. II, 1501); that the gas through line G goes through a gasoline plant, (R. II, 1501); that the introduction of inert gas at Joshua changes the specific gravity, (R. II, 1501); that the specific gravity of

the gas produced in the Panhandle field and in the several Oklahoma fields was approximately .63 (R. II, 1506); that a curve was made for each month principally because the specific gravity of the West Texas gas varies by a few points each month during the year and it was therefore necessary to determine the average specific gravity of the West Texas gas by months and plot a curve for each month instead of making a curve that might apply for a year, (R. II. 1507); that Fort Worth and Dallas, Texas, are furnished commingled gas at certain measuring stations and at other measuring stations wholly gas produced in Central West Texas, (R. V, 3228, 3229), that corrections had to be made for unaccounted for gas (R. V, 3221); that gas being compressible it does not follow Boyle's law exactly, (R. II, 1511). The above will suffice to show the intricacies through which the calculations must be carried to make a segregation by the specific gravity method. But this is not all. Schmidt further testified as follows: On line C-2 during the months of January, February, March, April, October, November, and December the specific gravity varied to such an extent that it was necessary to take daily averages of the specific gravity, (R. V, 3218), thus showing how unreliable the readings were for showing the true proportions of West Texas gas on the one hand and the indistinguishable Oklahoma-Texas Panhandle gas on the other hand. Similarly, for line E, (R. V, 3219). Similarly for Line F, (R. II, 3220). But further steps are outlined. The sales must be allocated by classes as between domestic and industrial gas. The witness testifies, due to the existence of these variable factors it was necessary to make

a determination by months of the relative volume of gas produced in the central West Texas area which had been sold at the domestic rate and the gas from the same area which had been sold at the industrial rate, (R. V, 3227). He testifies the metropolitan area of the city of Dallas received its supply of gas from 5 points of delivery, (R. V, 3229). Similarly for Fort Worth, (R. V, 3229). It will be noted from the charts shown at R. V, 3267 to 3278 that for a resulting specific gravity in the main of .80 the percentage of West Texas gas varies from approximately 79 per cent, (R. V, 3271) to 100 per cent (R. V, 3267). In other words, a specific gravity of .80 in the resulting mixture could mean a variation of 25 per cent in the amount of the West Texas gas.

Hulcy sponsored in evidence Company Exhibit 46 which purports to be a segregation of the property, revenues and expenses bottomed upon Company Exhibit 45. If the method of segregation adopted in Company Exhibit 45 falls down then the segregation of revenues, expenses, and property bottomed upon Company Exhibit 45 must fall also.

Even if the method of segregation were proper (which we do not concede) the year 1933 being an abnormally warm year (R. III, 1594-1595) as well as a "depression year," does not furnish a sufficient "spread of years" for adequate study. See cases cited under our Point XXXVI, infra.

A single illustration will suffice to show the degree of variation from day to day, by manipulation or otherwise, to which such a segregation is subject. At

Record V, 3241, Central Station, Dallas, on Line C, it is shown that on January 24, 1933, 13,604 MCF were measured at this station, all (100%) of which was West Texas gas. At Record V, 3242, March 2, 1933, the total gas measured at this station was 13,492 MCF, of which only 48% was West Texas gas. In other words, for the same total volume of gas the Company can at its own will and direction change the proportions of West Texas gas from 100% to as low as 48%.

We have heretofore pointed out Dunn's testimony that he is solely responsible for the sources, withdrawals, and direction of the gas in the system. R. I, 531. It is also significant to note Hulcy's testimony (R. I, 376) that direction of flow of the gas is continually reversing and shifting all over the system.

We point out also that it is conclusively shown that throughout the Commission hearings the Company was "lying low" before the Commission about the interstate commerce defense, while busily engaged in taking these gravitometer tests (of which it did not advise the Commission), and all the time the Company was preparing the data to spring for the first time in court. The order for the Commission's investigation served upon the Company was dated October 14, 1932, the hearing began November 1, 1932, and the Commission's order was dated September 13, 1933, R. I, 15, 116. It will be observed that the beginning of these gravitometer tests was January 1, 1933, and continued through that calendar year, R. V, 3241. The tests were made daily and continuously during the year. Although the hearings be-

fore the Commission continued until June 29, 1933, (R. I, 16), the Company made no disclosure before the Commission of its plan of making the gravitometer tests, nor of the results thereof. This shows plainly that this whole scheme was concocted after the Company learned of the pending rate investigation, and was carefully concealed from the Commission until its order was entered, and until the Company launched its attack upon the order on the ground of interstate commerce in the District Court for the first time in 1934.

Furthermore, the Company's exhibits and testimony show that while there were only 11 or 12 gravitometer test stations used, they were placed only at Gainesville and Petrolia, and the remainder grouped immediately around Dallas and Fort Worth. R. V, 3209-3222, map R. V, 3208A. No such tests were made at each of the city gates within the area in which the Company claims to have served mixed gas. And the Company throws no light upon why it chose and grouped the particular points for these tests as it did.

Hulcy was apparently not satisfied with the results of his labors; for, while he testified that it would be impossible to fix a separate gate rate for each town, (R. I, 376), he does in effect attempt by his segregation to do so upon a much more complicated and unreliable basis in "Area C" in which mixed gas is served.

This matter of "Area C" requires explanation. In the Company's testimony in explanation of its exhibit 46 (R. II, 1530-1567) Hulcy outlined areas A, B and C. "Area" and "Zone" are used synonymously

in the record and the map attached hereto as an appendix. Area A was the area covering the greater part of the Company's system in Texas within which it admitted that its operations were purely intrastate and subject to state regulation. Area B embraced the whole of Oklahoma and that portion of Texas served by Line A, west and north of Petrolia, within which area the Company claimed its operations were beyond state control. Area C embraced the relatively small zone in north central Texas within which it claimed to serve a mixture of Oklahoma, Texas Panhandle, and West Texas gas. Based upon these three areas, Hulcy worked out what he denominated D and E operations. D operations represented those which according to the Company's segregation embraced all property and operations in Area A plus an allocated portion of same in Area C; and E operations embraced all property and business in Area B plus the remaining parts of those in Area C. R. V, 3280.

In the Appellant's brief in the Court of Civil Appeals and in its application for writ of error to the Supreme Court of Texas, it attached as appendices a map in color with the lines of these respective areas plainly delineated. The colored map did not appear in the record. For some reason, the Company has not attached to its brief in this Court the map colored and with the areas delineated as it did in the state appellate courts. The map attached to its brief in this Court is the same map, but with the colored area lines and delineations obliterated. If the Court will hold the Company's map up to the light, it will see faint traces, similar to water marks, where these area lines

have been deleted, as has also been the legend which appeared in the upper right hand corner. For the Court's enlightenment, we have had the map, as it appeared in the Company's briefs in the state appellate courts, reproduced and attached as an appendix to this brief.

It conclusively appears that, aside from all other objections to this totally unreliable method of segregation, the results are not determinative at all of the proportions of West Texas gas on the one hand and the Texas Panhandle and Oklahoma gas on the other hand, served at each of the city gates, in Area C, and a very clear illustration of this fact is shown by the following circumstances:

Gas from West Texas is fed into Line F from the south. Gas from Oklahoma is fed into this line from the north during a part of the time. See map, R. V, 3208-A. The specific gravity measurements on this line were made on the McKinney tap, a tap line off the main line, about midway of Line F. There are some 15 cities and towns fed with gas from this line, and the proportions of West Texas, Texas Panhandle and Oklahoma gas respectively could vary considerably from the proportions measured at McKinney.

Aside from all other fatal objections to this method there is also the fundamental one that because of the Company's inability to determine by the gravity tests what proportions were Oklahoma gas as distinguished from Texas Panhandle gas, the segregation is wholly worthless if our contention be sound, as we think it is,

that the gas through Line A from the Texas Panhandle field is not transported in interstate commerce. R. II, 1497-1529; I, 230-231.

Contrast with the complicated, unreliable and inexact segregation made by the Company, the segregation made by Appellees in the District Court. The properties were divided according to the geographical location; that is, properties in Texas were allocated to Texas, and properties in Oklahoma were allocated to Oklahoma, except for Line A which was allocated wholly to Texas inasmuch as it brings gas from the Texas Panhandle across a corner of Oklahoma back into Texas. The revenues and expenses were divided on the same geographical basis. The net amount of Oklahoma gas brought into Texas was allowed for at the connecting point near the state line, at the average sale price for this gas in Texas. This net amount of Oklahoma gas brought into Texas was determined by deducting the amount of gas crossing the line into Oklahoma from the amount of gas crossing the state line from Oklahoma into Texas, R. III, 1736, 1737, 1748, 2124-A, 2142, 2157. This Court has approved such a geographical-and-use segregation in *Wabash Valley Elec. Co. vs. Young*, 287 U. S. 488, 495-497, 77 L. Ed. 447, 453.

Commission witness Phillips, in Ex. 4, (R. [redacted] 1632-1638, 1679-1683) directly allocated the operating revenues and expenses to Texas and Oklahoma respectively, and found that they substantially coincided with the proportions shown by the witness Freese in segregating the physical properties.

DIVISION B

CLAIMED DENIAL OF "ADEQUATE JUDICIAL REVIEW"

At page 126 of its brief, Appellant admits that it was not denied an "independent judgment as to the facts" by the District Court, or by the Court of Civil Appeals. Therefore, the doctrine of such cases as *Ohio Valley Water Co. vs. Ben Avon Borough*, 253 U. S. 287; *Bluefield Water Works & Imp. Co. vs. Public Service Commission*, 262 U. S. 679, 692, 693, and *St. Joseph Stockyards Co. vs. United States*, 298 U. S. 38, 51; and the *dictum in B. & O. R. Co. vs. United States*, 298 U. S. 349, 368, goes out of the case entirely.

The essence of Appellant's complaint as to denial of procedural due process under the Fourteenth Amendment, as stated at page 127 of its brief, is that by the judgment of the Court of Civil Appeals (and, incidentally that of the Supreme Court of Texas) it was denied "an adequate judicial review of the rate order." In subsequent argument in the brief, specifications are made that this claimed denial of adequate judicial review consisted in the judgment that the evidence as a whole was legally insufficient to overturn the presumed validity of the Commission's order, or to raise any issues of fact as to confiscation under the Federal Fourteenth Amendment to be resolved by the triers of fact.

Most of Appellant's complaint is directed at the *language and reasoning* of the Court of Civil Appeals in its opinion; more especially that to the effect that where the evidence is merely conflicting, and the reduced rate has not been given a reasonable test in

actual operation, the Court is not justified in overturning the Commission's order.

But here again, as was so aptly said by this Court in *United Gas Public Service Co. vs. Texas*, ____ U. S. ____, 82 L. Ed.____ (No. 13, Oct. Term, 1937):

> "We must distinguish 'between what was said and what was done,' between 'dictum and decision,' between reasoning and conclusion. *Dayton Power & Light Co. vs. Public Utilities Commission*, 292 U. S. 290, 298, 302."

Regardless of the reasoning of the Court of Civil Appeals in its opinion, what it in essence did was to analyze all of the evidence and to determine and adjudge, based upon such analysis, that the same did not as a matter of law possess sufficient legal probative force to overturn the *prima facie* validity of the Commission's order, or to raise any issues of fact as to unreasonableness and unjustness, or confiscation under the Federal Fourteenth Amendment; and that, for that reason, there were no fact issues raised to go to the jury as triers of fact. R. III, 3335, 3353, 3354, 3357, 3559-3370, especially 3369. For that reason, the Court very properly disregarded the verdict of the jury and reversed the judgment of the District Court, dissolved the injunction and upheld the rate order as having successfully withstood attack.

This *judgment* of the Court of Civil Appeals, affirmed by the Supreme Court of Texas, was a correct one, arrived at by well-established legal methods often sanctioned and applied previously in the decisions both of our highest state courts and of this Honorable Court.

In *Railroad Commission of Texas vs. Shupee*, 57 S. W. (2d) 295, 301 (affirmed by the Supreme Court of Texas, 123 Tex. 521, 528, 73 S. W. (2d) 505, 508) the same able Court of Civil Appeals from whence this appeal comes, in construing a statute in all substantial respects identical with Article 6059 (see appendix at end of this brief) relating to appeals to the courts for judicial review of the Railroad Commission's orders, said:

> "The manifest difference in these statutes is only as to the quantum of proof necessary on the respective appeals, and does not affect the principle on which the court acts in determining whether the order is unreasonable and unjust as to complainant, which rule is the same in each appeal. That is, each of these appeal statutes is construed with reference to the particular statutes to which each relates, and merely requires that the court must *first* judicially determine whether the complainant has introduced evidence of such probative force or value, or such character or quantum, as will satisfy the statutory burden placed by each statute upon the complainant; and when the court has judicially determined such matter favorably to complainant, *then to proceed with the trial of any fact issue as in ordinary trials on a preponderance of the evidence.*"

This is a succinct statement of the principle *applied* by the Court of Civil Appeals and the Supreme Court of Texas in this case, regardless of what else in addition was said in the opinion, and shows plainly that had Appellant's evidence been sufficiently "clear and satisfactory" or "clear and convincing" to hurdle the well established preliminary legal test, the court

would have been justified in submitting the fact issues, which would in that event have been raised, to the jury.

The principle has become staunchly established in the jurisprudence of our state in such decisions as *Railroad Commission of Texas vs. Galveston Chamber of Commerce,* 105 Tex. 101, 115, 145 S. W. 573; *Railroad Commission of Texas vs. Weld & Neville,* 96 Tex. 394, 409; 73 S. W. 529; *G. C. & S. F. Ry. Co. vs. Railroad Commission of Texas,* 102 Tex. 338, 352, 113 S. W. 741, 747; *Brown vs. Humble Oil & Refining Co.,* 126 Tex. 296, 87 S. W. (2) 1069, and many others.

Furthermore, the principle has received sanction and has been applied by this Honorable Court in a line of rate cases too numerous for us to cite. One of the latest and clearest enunciations of the principle by this Court is in *St. Joseph Stockyards Co. vs. United States,* 298 U. S. 38, 53, 80 L. Ed. 1033, 1042, as follows:

> "But this judicial duty to exercise an independent judgment does not require or justify disregard of the weight which may properly attach to findings upon hearing and evidence. On the contrary the judicial duty is performed in the light of the proceedings already had and may be greatly facilitated by the assembly and analysis of the facts in the course of the legislative determination. Judicial judgment may be none the less appropriately independent because informed and aided by the sifting procedure of an expert legislative agency."

The principle was also well stated and appropriately applied by this Court in the Laredo case (*United Gas Public Service Co. vs. Texas*) supra, as follows:

> "This Court will review the findings of fact by a State court . . . (2) where a conclusion of law as to a Federal right and findings of fact are so intermingled as to make it necessary, in order to pass upon the Federal question, to analyze the facts . . . we make that analysis, not to determine issues of fact raised on conflicting testimony or inferences, and thus to usurp the function of the State court as a trier of the facts, but to perform our own proper function in deciding the question of law arising upon the findings which the evidence permits."

The cases cited under our Point XXXIX, infra, show that expert testimony, of which this record is almost wholly made up, has in law no probative force, and is "in no real sense evidence," unless it is "clear and satisfactory" or "clear and convincing" in the sense that it is reasonable and based upon satisfactory basic factual data. The Company's evidence here is clearly insufficient as a whole to meet that test, and was therefore properly rejected.

This principle has been applied by this Court also in such decisions as *San Diego L. & T. Co. vs. National City*, 174 U. S. 739, 754, 43 L. Ed. 1154; *Darnell vs. Edwards*, 244 U. S. 564, 569, 61 L. Ed. 1317; *Willcox vs. Consolidated Gas Co.*, 212 U. S. 19, 41, 53 L. Ed. 382; *Louisville vs. Cumberland Tel. & Tel. Co.*, 225 U. S. 430, 433, 436, 56 L. Ed. 1151; *Norfolk & W. R. Co. vs. North Carolina*, 297 U. S. 682, 689-690, 80 L. Ed. 977; *Brush Electric Co.*

vs. Galveston, 262 U. S. 443, 444-446, 67 L. Ed. 1076; *Lincoln G. & E. Co. vs. Lincoln*, 250 U. S. 256, 261-262, 268, 63 L. Ed. 968; *Cedar Rapids Gas Co. vs. Cedar Rapids*, 223 U. S. 655, 667-670, 56 L. Ed. 594; *Galveston Electric Company vs. Galveston*, 258 U. S. 388, 401, 403, 66 L. Ed. 678; and many others.

In short, what the highest courts of our State have done in this and other cases, and what this Court has done in the above cited cases and many others, is to analyze the evidence and determine as a preliminary law question whether the elaborate theories, calculations, speculations, tabulations, estimates and prophecies of the expert witnesses testifying for the complaining utilities, were based upon sufficiently sound underlying basic factual data to possess enough probative force to overturn the *prima facie* validity of the rate order, and to raise issues of fact to be resolved; in other words, whether such evidence is sufficiently "clear and satisfactory" to raise fact issues of unreasonableness and unjustness under the state law and decisions, or sufficiently "clear and convincing" to demonstrate confiscation under the Federal Fourteenth Amendment. If this preliminary law question be determined in the negative, then there are no fact issues to pass upon.

The Court of Civil Appeals and the Supreme Court of Texas were not examining the evidence with a view, primarily, of resolving any fact issues and making original fact findings of their own, but were doing precisely what this Court has said in the above quoted excerpt from the Laredo case it may properly do, namely,

sifting the evidence with a view of determining what fact findings if any, the evidence *would be sufficient to support;* and, having determined this, to decide the law question as to whether the evidence was "clear and satisfactory" or "clear and convincing." The issues have both been properly resolved against Appellant by the state appellate courts in this case.

In making the contention that the highest state courts have by this legal *modus operandi* denied it due process under the Federal Fourteenth Amendment, the Appellant is necessarily arguing impliedly that this Honorable Court has by that identical legal method denied many litigants due process under the Fifth Federal Amendment in the numerous decisions of this Court above cited, and many others.

This contention of Appellant necessarily resolves itself into a question simply of the correctness, as a law question, of the highest State courts' action in adjudging that the evidence was legally insufficient, and lacked the necessary quality of being "clear and satisfactory", and "clear and convincing" to raise fact issues of confiscation, etc.

If this determination by the state courts was error at all, it was necessarily either an error of state law or of Federal law. If it was merely an error of state law, this Court does not concern itself with the question. If it was an error of Federal law, then this Court has the entire record before it, and will, as it has so often done, exercise its undoubted privilege of analyzing the evidence and determining what fact findings, if any, the evidence would have been sufficient to support, and then, based upon this determination, decide

further the legal question of whether confiscation under the Fourteenth Amendment has been shown by that "clear and convincing evidence" which this Court has so often held to be indispensable to demonstrate denial of Federal rights. This Court not only has the power to do so, but we gladly invite it to do so.

Appellant contends in effect that it has been deprived of a jury trial. But this raises no question of federal right; for, in the first place, no assignment is made that the Seventh Federal Amendment has been violated; and, in the second place the amendment has no application in cases arising in the state courts. *Minn. & S. L. R. Co. vs. Bombolis*, 241 U. S. 211, 60 L. Ed. 961. Neither does the Fourteenth Federal Amendment guarantee a trial by jury: *Walker vs. Sauvinet*, 92 U. S. 90, 23 L. Ed. 678; *Maxwell vs. Dow*, 176 U. S. 581; *Frank vs. Mangum*, 237 U. S. 309.

There is nothing in the Federal Constitution which requires a state to maintain the distinction between the functions of the jury and that of the court; it may do away with the jury altogether: *C. R. I. & P. R. Co. vs. Cole*, 251 U. S. 54, 64 L. Ed. 133. *Palko vs. Connecticut*, ____ U. S. ____, 82 L. Ed. ____, No. 135, Oct. Term, 1937, L. Ed. Adv. Op. No. 5, p. 220, 223.

The principle applied by the Court of Civil Appeals and the Supreme Court of Texas in disposing of this case, is actually nothing more than a mere adjective or procedural rule of evidence or burden of proof applied in obedience both to a state statute (Art. 6059) and the decisions of this Court. The Federal Fourteenth Amend-

ment does not guarantee one the benefit of a mere rule of evidence. A right to have one's controversies determined by the existing rules of evidence is not a vested right, for such rules pertain to the remedies which the state provides for its citizens, and generally they neither enter into and constitute a part of any contract, nor can they be regarded as being of the essence of any right which a party may seek to enforce: *Luria vs. United States*, 231 U. S. 9, 58 L. Ed. 101.

Appellant insists that the jury has in its verdict found that the 32c rate is *confiscatory*, within the prohibition of the Federal Fourteenth Amendment. This argument is predicated upon this Court's holding in the Laredo case that the issue of confiscation had been submitted and found against the United Gas Company in that case, but that here the issue has been submitted and resolved against the Commission. The argument is plausible but specious; and the conclusion does not necessarily follow the premises. Since the line of *reasonableness* (a question of state law) is higher than the line of confiscation (a matter of Federal law), a finding (as in the Laredo case) that the reduced rate is *reasonable* necessarily means that it is non-confiscatory; but the converse is not true. A finding (as here) that the rate is *unreasonable* does not necessarily imply at all that it is *confiscatory*.

Thus the question of claimed denial of "adequate judicial review" disappears and merges itself into the question of whether the record shows confiscation by the requisite degree of clearness. And to this latter question the remainder of this brief will be addressed.

DIVISION C

CLAIMED CONFISCATION

GENERAL THESIS: APPELLANT'S EVIDENCE AS A WHOLE WAS INSUFFICIENT AS A MATTER OF LAW TO DEMONSTRATE CONFISCATION OR OTHER DEPRIVATION OF FEDERAL CONSTITUTIONAL RIGHT, AND TO OVERTURN THE PRESUMED VALIDITY OF THE ORDER. THIS BECOMES MORE CLEARLY EVIDENT WHEN APPELLANT'S EVIDENCE IS CONSIDERED IN CONNECTION WITH, AND CHECKED BY, APPELLEES' COUNTERVAILING EVIDENCE AS TO THE COMPENSATORY CHARACTER OF THE RATE. HOWEVER, THE VOLUNTARY AND UNNECESSARY SUBMISSION OF SUCH EVIDENCE BY APPELLEES DID NOT HAVE THE LEGAL EFFECT OF LIFTING THE BURDEN FROM APPELLANT OF PROVING BY ITS OWN EVIDENCE A CLEAR AND CONVINCING CASE OF CONFISCATION OR OTHER FEDERAL CONSTITUTIONAL INVALIDITY.

XXV. The order is presumed *prima facie* to be non-confiscatory and valid:

R. R. Com. of Cal. vs. Pacific G. & E. Co., ... U. S. ....., 82 L. Ed. ....., No. 804, Oct. Term, 1937, Adv. Op. No. 7, p. 327;

St. Joseph Stockyards Co. vs. United States, 298 U. S. 38, 52, 53, 54, 60, 64, 67; 80 L. Ed. 1033, 1041, 1042-1043, 1046, 1048, 1049;

Lindheimer vs. Ill. Bell Tel. Co., 292 U. S. 151, 164, 169, 175; 78 L. Ed. 1182, 1191, 1193, 1194, 1197;

Los Angeles G. & E. Corp. vs. R. R. Com. of Cal., 289 U. S. 287, 304, 305, 307; 77 L. Ed. 1180, 1192;
Dayton P. & L. Co. vs. Pub. Ut. Com. of Ohio, 292 U. S. 290, 298; 78 L. Ed. 1267, 1274;
Darnell vs. Edwards, 244 U. S. 564, 569; 61 L. Ed. 1317, 1321;
Willcox vs. Consolidated Gas Co., 212 U. S. 19, 41; 53 L. Ed. 382, 395;
United Fuel Gas Co. vs. R. R. Com. of Kentucky, 278 U. S. 300, 313; 73 L. Ed. 390, 398.

XXVI. Orders of the Commission have the same force and effect as ordinary statutes of the State; and are, therefore, entitled to the exceedingly strong presumption of validity that is accorded to statutes in determining the constitutionality thereof:

Pacific States Box & Basket Co. vs. White, 296 U. S. 176, 185-186; 80 L. Ed. 138, 146;
West Texas Compress Co. vs. P. & S. F. Ry. Co., 15 S. W. (2) 558, 560;
R. R. Com. of Texas vs. Uvalde Construction Co., 49 S. W. (2) 1113, 1114.

XXVII. The burden is upon the complaining party to prove confiscation or deprivation of other constitutional rights by evidence so clear and satisfactory as to leave no reasonable doubt in the judicial minds of the reviewing courts:

Cases cited under Point XXV above; and
Art. 6059 R. C. S. Tex. (1925);[7]

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[7]"In all trials under this article the burden of proof shall rest upon the plaintiff, who must show by CLEAR AND SATISFACTORY evidence that the rates . . . complained of are unreasonable and unjust to it or them."

R. R. Com. of Cal. vs. Pacific G. & E. Co. No. 804, Oct. Term, 1937, ... U. S. ....., 82 L. Ed. ....., L. Ed. Adv. Op. No. 7, p. 327, 334.
United F. G. Co. vs. R. R. Com. of Ky., 278 U. S. 300, 313, 73 L. Ed. 390. 398;
San Diego Land & Town Co. vs. National City, 174 U. S. 739, 754; 43 L. Ed. 1154, 1160;
Knoxville vs. Knoxville Water Co., 212 U. S. 1, 16; 53 L. Ed. 371, 381;
C. M. & S. P. R. Co. vs. Thompkins, 176 U. S. 167, 173; 44 L. Ed. 417, 420;
G. C. & S. F. Ry. Co. vs. R. R. Com. of Texas, 102 Tex. 338, 352; 113 S. W. 741, 747, 795;
R. R. Com. of Tex. vs. Weld & Neville, 96 Tex. 394, 409; 73 S. W. 529;
R. R. Com. of Tex. vs. Galveston Chamber of Commerce, 105 Tex. 101, 115; 145 S. W. 573.

XXVIII. The foregoing rule (XXVII above) does not place upon the Company, as it contends, an impossible burden in the sense that the order will be upheld if there is any evidence countervailing against the Company, R. V, 3351. It does mean that the Court of Civil Appeals, and the Supreme Court of Texas, properly did what this Court has many times done, namely, analyzed all of Appellant's evidence and determined as a preliminary law question that the same lacks the quality of being sufficiently "clear and satisfactory" or "clear and convincing" to outweigh the presumed validity of the order. The law itself, which places upon one complaining of the Commission's order the extraordinarily heavy burden of proving it confiscatory by clear and convincing evidence, stands always at the threshhold of a rate case as a continuing challenge of the legal sufficiency of the complaining

party's evidence to raise issues of fact. If the evidence does not measure up to that required standard, in the opinion of the reviewing courts sitting in chancery (this being an equity case), then the complaining party has, as a matter of law, failed to discharge the burden of overturning the order. The complaining party proceeds at his own peril as to meeting this burden. Any other rule would make the courts, and not the Commission, the ultimate legislative rate-makers. *St. Joseph Stockyards Co. vs. United States,* 298 U.S. 53, 80 L. Ed. 1033, 1041.

XXIX. The complaining party does not meet the burden of proving the invalidity of the order by attacking the evidence adduced by the opposing party, but must himself submit evidence sufficiently clear and satisfactory to overturn the order:

Allen vs. S. L. I. M. & S. Ry. Co., 230 U. S. 553, 560; 57 L. Ed. 1625, 1629;
Atlantic Coast Line R. Co. vs. Florida, 295 U. S. 301, 317-318; 79 L. Ed. 1451, 1461-1462;
Norfolk & W. Ry. Co. vs. North Carolina, 297 U. S. 682, 689-690; 80 L. Ed. 977, 982-983.

XXX. This Court has been especially reluctant to find rates confiscatory where, as here, they have not been put into effect and given a reasonable trial in actual operation, to eliminate speculation and to determine definitely the volume of business and net revenue that would be produced under the reduced rates:

Knoxville vs. Knoxville Water Co., 212 U. S. 1, 16-17; 53 L. Ed. 371, 381-382;
Darnell vs. Edwards, 244 U. S. 564, 569; 61 L. Ed. 1317, 1321;

Willcox vs. Consolidated Gas Co., 212 U. S. 19, 41; 53 L. Ed. 382, 395;
Georgia Power Co. vs. R. R. Com. of Georgia, 262 U. S. 625, 633; 67 L. Ed. 1144, 1148;
St. Joseph Stockyards Co. vs. United States, 298 U. S. 38, 49, 72; 80 L. Ed. 1033, 1040, 1052;
Louisville vs. Cumberland Tel. & Tel. Co., 225 U. S. 430, 433, 436; 56 L. Ed. 1151, 1152;
Brush Electric Co. vs. City of Galveston, 262 U. S. 443, 444-446; 67 L. Ed. 1076, 1077-1078;
Lincoln G. & E. Co. vs. Lincoln, 250 U. S. 256, 262; 63 L. Ed. 968, 974;
Cedar Rapids Gas Co. vs. Cedar Rapids, 223 U. S. 655, 667-670; 56 L. Ed. 594, 603-604;
S. & N. Ala. Ry. Co. vs. R. R. Com. of Ala., 210 Fed. 465, 480.

XXXI. If Appellant had put the 32c rate into effect promptly upon promulgation of the order and had given it a reasonable test or trial period, and thus enabled its *alter egos*, the affiliated distributors, to carry the saving into the burner tip rates to the consumers, as it should have done instead of defying the order and choosing rather to assert its unconstitutionality in all the courts of the land, it is probable, if not certain, under the record here, that an increased attachment of new customers and an increased consumption per customer on the Lone Star group's entire integrated system would have resulted, which long before now would have more than offset in increased net revenue to the group the amount of the reduction:

Louisiana R. Com. vs. Cumberland Tel. & Tel. Co., 212 U. S. 414, 426; 53 L. Ed. 577, 583;
Willcox vs. Consolidated Gas Co., 212 U. S. 19, 49-50; 53 L. Ed. 382, 398;

Knoxville vs. Knoxville Water Co., 212 U. S. 1, 16; 53 L. Ed. 371, 381;
Brush Electric Co. vs. Galveston, 262 U. S. 443, 446; 67 L. Ed. 1076, 1078.

XXXII. This Court is not concerned with mere irregularities or erroneous methods or reasoning pursued by the Commission, or by the State courts, but is interested only in determining whether the prescribed rate in its over-all result ("totality of its consequences") falls below the line of confiscation:

R. R. Com. of Cal. vs. Pacific G. & E. Co. No. 804, Oct. Term, 1937, ____ U. S. ____, 82 L. Ed. ____ (L. Ed. Ad. Op. No. 7, p. 327, decided Jan. 3, 1938);
Los Angeles G. & E. Corp. vs. R. R. Com. of Cal., 289 U. S. 287, 304-305, 314, 315-316, 317; 77 L. Ed. 1180, 1192, 1197, 1198, 1199;
Lincoln G. & E. Co. vs. Lincoln, 250 U. S. 256, 267-268, 63 L. Ed. 968;
Dayton P. & L. Co. vs. Pub. Ut. Com. of Ohio, 292 U. S. 290, 297-298, 309; 78 L. Ed. 1267, 1274-1280;
Lindheimer vs. Ill. Bell Tel. Co., 292 U. S. 151, 175; 78 L. Ed. 1182, 1197;
St. Joseph Stockyards Co. vs. United States, 298 U. S. 38, 49, 69; 80 L. Ed. 1033, 1040, 1050;
W. Ohio Gas Co. vs. Pub. Ut. Com. of Ohio (Lima Case), 294 U. S. 63, 70; 79 L. Ed. 761, 768;
R. R. Com. of Texas vs. Galveston Chamber of Commerce, 105 Tex. 101, 115-116, 145 S. W. 573, 580.

XXXIII. A corollary is, that even should it be proved that the Commission has made a finding er-

roneously prejudicial to the Company as to some particular element or elements of the rate structure (which was not done here), the Company must go farther and prove that other compensating liberalities have not been indulged in its favor by the Commission in the findings and allowances as to other elements of the rate structure:

R. R. Com. of Cal. vs. Pacific G. & E. Co. No. 804, Oct. Term, 1937, ... U.S. ....., 82 L. Ed. ..... (L. Ed. Adv. Op. No. 7, p. 327, decided Jan. 3, 1938);

Los Angeles G. & E. Corp. vs. R. R. Com. of Cal., 289 U. S. 287, 316-317; 77 L. Ed. 1180, 1198-1199;

Lindheimer vs Ill. Bell Tel. Co., 292 U. S. 151, 175; 78 L. Ed. 1182, 1197;

Dayton P. & L. Co. vs. Pub. Ut. Com. of Ohio, 292 U. S. 290, 305, 306, 309-310; 78 L. Ed. 1267, 1278, 1279, 1280-1281;

Lincoln G. & E. Co. vs. Lincoln, 250 U. S. 256, 267-268; 63 L. Ed. 968, 976.

XXXIV. All of the Company's claims of confiscation are bottomed upon the fallacious assumption that the average 6% net annual return fixed by the Commission, and all of its other findings as to rate base and other elements and subsidiary facts relating to the rate structure, insofar as such findings are favorable to the Company, are sacred and inviolable minima below which the Commission and the reviewing courts are estopped and precluded from going in determining the issue of confiscation; and that, insofar as such findings are unfavorable to the Company, they are subject to its attack. No estoppel or *res judicata* is involved in connection with the find-

ings, either of the Commission or of the inferior reviewing courts. If the Company is free to attack the findings, as being too low, then the Commission must be equally free to show that they are too liberal:

St. Joseph Stockyards Co. vs. United States, 298 U. S. 38, 46-47, 56, 63-64, 72; 80 L. Ed. 1033;

Lindheimer vs. Ill. Bell Tel. Co., 292 U. S. 151; 78 L. Ed. 1182;

Columbus Gas & Fuel Co. vs. Pub. Ut. Com. of Ohio, 292 U. S. 398, 414; 78 L. Ed. 1327, 1336;

Prentis vs. Atlantic Coast Line R. Co., 211 U. S. 210, 227; 53 L. Ed. 150, 159;

XXXV. The Company's claims of confiscation are likewise founded upon the erroneous assumption that unreasonableness (which is here a question of State law) is the same thing as confiscation, which is a Federal question. The issue before this Court is not whether the 32c rate will yield 6%, or any other reasonable rate of return, but whether it is confiscatory. This distinction should be borne in mind in reading the precedents. Some cases previously before this Court, coming up from inferior Federal Courts, have involved both confiscation and unreasonableness.

XXXVI. All of the Company's claims of confiscation are built also upon the untenable assumption that if it be shown that the net revenues under the reduced rate for any particular twelve-months' operating period would, under the basic findings of the Commission, apparently have fallen below the average 6% level fixed by the Commission, upon a theoretical application of the 32c rate to the volume

of business actually enjoyed in the past under the 40c rate, that this, *ipso facto*, shows confiscation. In attempting to make such a showing, the Company insisted before the Commission that the latter, in fixing the rate, should only use the operating results for the years 1931-1932, during which years the revenues were indisputably deeply affected by the economic depression; and, before the courts, that the validity of the rate should be tested only by the operating results of depression years, including 1933, which year was admittedly and indisputably doubly abnormal because of the depression and the unsually high temperatures. This method was erroneous, first, for insisting upon confining the investigation before the Commission to too short a test period, which is condemned by all of the authorities, regardless of abnormalities; and, second, for attempting to have the rate fixed and tested by the results of operating periods which were abnormal for two different reasons, each year resting upon its own bottom without considering the average results of any spread of years. The authorities amply establish that the Commission, in fixing the rate, and the Courts, in testing it, both for unreasonableness and confiscation, should not limit their vision to a single twelve-months' operating period, or even two consecutive abnormal operating periods, but should consider the *average results* of a reasonable spread of fat and lean years, in order to equalize the fluctuations inevitably brought about by abnormalities of every kind:

United Gas Pub. Serv. Co. vs. State of Texas, ____ U. S. ____, 82 L. Ed. ____, L. Ed. Adv. Op. No. 10, 490, 500, 502, Feb. 14, 1938.

Louisville vs. Cumberland Tel. & Tel. Co., 225 U. S. 430, 433, 436, 56 L. Ed. 1151;

Los Angeles G. & E. Corp. vs. R. R. Com. of Cal., 289 U. S. 287, 298-299, 303-304, 311-312, 319-320; 77 L. Ed. 1180;
St. Joseph Stockyards Co. vs. United States, 298 U. S. 38, 46-47, 55, 71, 72; 80 L. Ed. 1033, 1038-1039, 1051-1052;
Lindheimer vs. Ill. Bell Tel. Co., 292 U. S. 151; 78 L. Ed. 1182;
Galveston Elec. Co. vs. Galveston, 258 U. S. 388, 400, 401, 403; 66 L. Ed. 678, 685, 686;
Lincoln G. & E. Co. vs. Lincoln, 250 U. S. 256, 268; 63 L. Ed. 968, 976;
Darnell vs. Edwards, 244 U. S. 564, 569; 61 L. Ed. 1317, 1321;
Brush Electric Co. vs. Galveston, 262 U. S. 443, 446; 67 L. Ed. 1076, 1078;
Knoxville vs. Knoxville Water Co., 212 U. S. 1, 14-15, 17-18; 53 L. Ed. 371, 380, 381, 382;
Acker vs. United States, 298 U. S. 426, 431; 80 L. Ed. 1257, 1261-1262;
West Ohio Gas Co. vs. Pub. Ut. Com. of Ohio (Kenton Case), 294 U. S. 79, 81; 79 L. Ed. 773, 776;
Municipal Gas Co. vs. Com. 225 N. Y. 89, 98; 121 N. E. 772, 774;
Denver Union Stockyards Co. vs. United States; 57 Fed. (2) 735, 752-753;
Kings County Lighting Co. vs. Lewis, 110 Miscl. Rep. 204; 180 N. Y. Suppl. 570, 593;
S. & N. Ala. Ry. Co. vs. R. R. Com. of Ala., 210 Fed. 465, 480;
Reno P. L. & W. Co. vs. Com., 298 Fed. 790, 801.

XXXVII. Obviously the Commission could not, and did not attempt to, prescribe any rate to be effective in Oklahoma, but only "within the jurisdiction of Texas." In order to prove the prescribed rate confisca-

tory when limited to and applied within Texas only, the burden devolved upon Appellant, and was not discharged, of submitting to the reviewing courts evidence sufficiently clear and satisfactory as a matter of law, to enable the courts to make a proper, reasonable, just, and practical segregation between Texas and Oklahoma properties and operations; otherwise, the probability was presented, and in fact this record made it a certainty, that the more expensive Oklahoma intrastate business would unduly raise and burden unjustly to Texas rate-payers, the cost of Appellant's intrastate business in Texas.

XXXVIII. The net annual rate of return, after due allowance for operating expenses and depreciation and depletion, which according to this record would probably have been earned by Appellant under the Commission's order, if it had been put into actual effect promptly when promulgated, and the rate of net return which under the record would probably be earned in the future according to this record, is not confiscatory when viewed in the light of economic conditions then and now prevailing:

Dayton P. & L. Co. vs. Pub. Ut. Com. of Ohio, 292 U. S. 290, 311, 78 L. Ed. 1267, 1281.

XXXIX. The weight to be accorded to the testimony of Appellant's experts cannot be determined without understanding their approach to the questions and the criteria which governed their estimates. The testimony of Appellant's witnesses shows quite clearly that in every essential element of the rate structure, both ultimate and subsidiary, and in many particulars, they proceeded, in part at least, upon erroneous,

conjectural, unfair, extravagant, speculative, and untenable bases in arriving at their estimates, opinions, conclusions, valuations, and prophesies. (See argument, infra, for details.) Their testimony and estimates are, therefore, to be rejected as having no probative force in law and as being "in no real sense evidence," in so many instances as to make the totality of Appellant's evidence fall far short of raising any fact issues as to confiscation:

St. Joseph Stockyards Co. vs. United States, 298 U. S. 38, 53, 54, 60, 64, 67, 59-60, 62, 63; 80 L. Ed. 1033, 1045, 1047;

Los Angeles G. & E. Corp. vs. R. R. Com. of Cal., 289 U. S. 287, 304, 305, 307, 317-319; 77 L. Ed. 1180, 1199-1200;

Dayton P. & L. Co. vs. Pub. Ut. Com. of Ohio, 292 U. S. 290, 298-301, 302, 305, 311-312; 78 L. Ed. 1267, 1274-1276, 1277, 1278, 1281, 1282;

Columbus G. & F. Co. vs. Pub. Ut. Com. of Ohio, 292 U. S. 398, 412-413; 78 L. Ed. 1327, 1335-1336;

Lindheimer vs. Ill. Bell Tel. Co., 292 U. S. 151, 162-164, 170-175; 78 L. Ed. 1182, 1189-1191, 1194-1197;

Knoxville vs. Knoxville Water Co., 212 U. S. 1, 18; 53 L. Ed. 371, 382;

United Fuel Gas Co. vs. R. R. Com. of Ky., 278 U. S. 300, 316-317, 73 L. Ed. 390, 399.

XL. The Appellant's attitude from the inception of this proceeding before the Commission has been one of studied concealment and distortion of the facts, and non-cooperation, rather than one of candid revelation. An examination of the entire record herein will show this to be true. The Company would much

better have served its own interests by aiding the regulatory authorities and the reviewing courts in arriving at the truth, rather than engendering lasting distrust by continuing attempts to distort the facts unreasonably in its own favor:

Knoxville vs. Knoxville Water Co., 212 U. S. 1, 18; 53 L. Ed. 371, 381-382.

XLI. The Appellant, in its evidence and computations presented before both the Commission and reviewing courts, has relied upon "elaborate tabulations of estimates," "at war with realities", which have "proved too much" and "overshot the mark." (See details set out in argument following.) "Men do not transact business without protest at confiscatory rates, at all events in the absence of extraordinary circumstances making submission to the loss expedient. If such circumstances exist, the Appellant has not proved them. . . That being so, what the public utility has done belies what it has said." If Appellant's own computations were given full faith and credit at their face value, and more especially if Appellant's own tests for determination of confiscation be adopted (as we think they should not be), they would reveal that for many years prior to the initiation of these proceedings, the Appellant had been doing business at its own 40c gate rate, voluntarily fixed and adhered to without any constraint upon the part of public regulatory authorities, and without asking for permission to raise the rate, at net rates of return which, according to the Company's own computations would apparently have been confiscatory. And, further, the indisputable facts in the record show that the 40c rate has been far

above the line of confiscation. This inherent vice in Appellant's contentions deprives them of all probative force for the purpose of establishing confiscation:

Dayton P. & L. Co. vs. Pub. Ut. Com. of Ohio, 292 U. S. 290, 311-312; 78 L. Ed. 1267;
Lindheimer vs. Ill. Bell Tel. Co., 292 U. S. 151, 161, 162, 163, 164, 175, 176; 78 L. Ed. 1182.

STATEMENT AND ARGUMENT UNDER POINTS NOS. XXV TO XLI

All we have said in Division A of this brief with reference to segregation as between Texas and Oklahoma properties and operations, and what Appellant contends are "interstate and intrastate" properties and operations on the other hand, is here adopted. We hope we have made our view sufficiently plain that we do not consider there are any interstate commerce operations involved here at all; and, therefore, no necessity or proper occasion for making any segregation as between interstate and intrastate commerce. That necessity would arise only if, and to the extent that, Appellant were correct in its contention that any part of its operations in Texas constitutes interstate commerce such as to be beyond the regulatory reach of the State of Texas. In our view, however, there was both necessity for and propriety in making a just, practical and reasonable segregation as between Oklahoma and Texas properties and operations in order that in testing the adequacy of the 32c gate rate in its operation as applied within Texas, the Texas consumers might not be required unjustly to bear the burden of the more expensive and less profitable operations in

Oklahoma, even though the Commission, in its desire to be more than just and generous both to the Company and to the consumers in Oklahoma, did see fit unnecessarily to fix the rate upon an over-all and unsegregated basis for application within Texas only. Such was the segregation voluntarily offered by the Appellees in the District Court.

By way of prelude we express our confidence that whether the adequacy of the rate as applied in Texas be determined upon an over-all Texas-Oklahoma basis (as fixed by the Commission and as contended for by the Company) or upon the basis of Appellees' segregation between Texas and Oklahoma properties and operations, or even upon the basis of the entirely unacceptable purported segregation between so-called "interstate and intrastate" operations submitted by the Company in the District Court, the rate will not be found confiscatory upon any basis.

To demonstrate this, we have inserted at the end of this brief our Tables I to V inclusive, the bases of which are stated in detail, infra pp. 189-192. It is pertinent in this connection to observe that in these Tables we have not deducted any of the improper operating expenses to which we object below, except management fees, and, in some cases, some of the donations. It is important also to observe that only a little more than six months elapsed between the effective date of the order (September 13, 1933) and latest operating statement appearing in the record (April 30, 1934). This is certainly too short a period by which to test the legality of a rate never put into operation. The Tables show that on any basis the average rate of return after application of the 32c rate is above 8%.

As pointed out in *Lindheimer vs. Ill. Bell Telephone* Co., 292 U. S. 151, 164, 78 L. Ed. 1182, 1191, the propriety of the items in Appellant's operating expense accounts may be quite as important a factor as the valuation of properties in the rate base. In fact, that is an understatement. As a matter of fact where the rate of return has been fixed at 6%, as here, a dollar in the operating expense account (and the same thing is true as to a dollar in the depreciation reserve accruals) possesses a ratio of importance 16.67 times as great as a dollar in the rate base; because each dollar of gross revenue charged to the depreciation reserve or the operating expense account takes away the equivalent of a 6% return for one year on $16.67.

For these reasons and because of the great sums claimed by Appellant as necessary for its annual depreciation reserve ($3,465,123.36 per annum for entire properties of Lone Star Gas Co. as of January 1, 1933, R. II, 1262, V, 3056) and for items of operating expenses of which we have questioned the propriety, we choose first to discuss the item of depreciation reserve; next, the questioned items of operating expense; then the elements in the rate base; then rate of return; and, last, the operating computations submitted by the Company and compared with those in our Tables I to V inclusive.

The Commission's Exhibit 5, (R. III, 2140-A) shows accurately the undepreciated historical book costs of the Company's entire properties as per its records for the years 1927, through the year ending March 31, 1934, at the maximum of $50,514,576.98 as of December 31, 1932. As against

this, the Company submitted its reproduction cost new estimate of $73,983,405.57, as of January 1, 1933, R. IV, 2363. These figures compare with the Commission's overall undepreciated rate base of $46,520,137.06, determined as of December 31, 1932, (R. I, 110); and with the undepreciated reproduction cost new estimates submitted by the Commission's witness, in the District Court, of $40,256,862.39, as of June 15, 1934, for the Texas segregated properties exclusive of production system, R. III, 2143.

Thus it will be seen that Appellant's witnesses have taken a $46,000,000.00 property and by some processes of legerdemain added to it an estimated additional inflation, undepreciated, of approximately $28,000,000.00. It is our purpose in the course of this discussion to expose some of the methods by which this astounding result was produced. These results were reached chiefly through the cooperative team work of the Company's talented galaxy of expert witnesses, Steinberger, Biddison, Connor, Hulcy, and Dunn. The division of labor between them was substantially as follows:. Steinberger supervised the taking of inventories, conducted certain "costs studies", the qualities of which we will touch upon in later passages, and served as cup-bearer to the witnesses Biddison, Hulcy, and Dunn. Steinberger and Biddison were largely responsible for the reproduction cost new estimates of the physical properties, or direct structural costs, totaling $50,813,515.57, R. IV, 2366. Geologist Kendrick, engineer Dunn, and accountant Hulcy made their contributions in estimates and evaluations of gas reserves. Engineer Connor added to the $50,000,000.00 of estimated

direct reproduction cost of physical properties and gas reserves a mere trifle of approximately $25,000,000.00 in claimed intangible values, consisting of preliminary and organization expense, engineering and supervision, interest during construction, taxes during construction, legal and administrative cost, working capital and going concern value. Connor also made a modest little estimate of $3,465,123.36, annual accruals to the depreciation reserve, although the actual charges to reserves as shown on the Company's books for seven years average only $344,871.84 per year, Table II, infra. Hulcy sponsored the accounting exhibits.

It would be utterly impossible for us to point out in a brief of reasonable length more than a few typical illustrations of the hundreds of erroneous and unjust methods used by the Appellant's witnesses in arriving at their estimates. But, when the Court reads the record, it will discover that on almost every page there appear one or more of these glaringly obvious inadmissible methods of treatment by the Company's experts. We believe the Court will be constrained at least to agree with the restrained understatement of the Court of Civil Appeals, when it said in its opinion, (R. V, 3369) that:

> "The calculations, estimates, and opinion of its experts show a studied effort on the part of Appellee to charge large items as operating expenses and depreciation, at war with the actual experiences of the Company, and we find no proof which would authorize the trial court to submit to the jury any issue, but find that Appellee wholly failed to meet the burden of proof

placed upon it, and to show by clear and satisfactory evidence that the rate was confiscatory, unjust, and unreasonable as to it."

The testimony shows that the estimates and methods of the Company's experts had absolutely no relation to reality or to the Company's actual experience; and that said witnesses were brazenly frank in stating that they had made no attempt to ascertain from the Company's records its actual experiences and history, or to relate their testimony and estimates in any way thereto; R. I, 662, 750.

ANNUAL ACCRUALS TO DEPRECIATION, DEPLETION AND AMORITIZATION RESERVES

Connor was the sole witness purporting to carry the burden for the Company upon this phase of the case, both before the Commission and the District Court. In the court trial, he sponsored Company Exhibit 42, consisting of a typewritten volume of 312 pages purporting to set forth the bases and methods of approach used in arriving at his conclusions and estimates. The contents of this tome, as well as Connor's oral testimony, are in part fantastic, in part unintelligible, in part audacious, in part merely erroneous, and in all parts highly inflated; bearing no relation to realities, and in no way fairly substantiated by the actual experience of the Company. We have not chosen to encumber the record before this Court by printing the whole of Connor's Exhibit 42, but have only given the Court a representative cross-section thereof in R. V, 3057-3196. His oral testimony with respect to these subjects will be found in R. II, 1256-1323,

1331-1434, 1452-1459; R. III, 1992-2002, 2029-2043. We ask the Court to refer to R. II, 1366-1368 for a representative sample of the meaningless abracadabra of which Connor's testimony, in large part, was made up. On cross-examination he could seldom, if ever, be forced into answering a question, but instead would evade it and launch out upon a long, rambling, unintelligible, pseudo-scientific treatise, remarkable chiefly for its inanity.

Mr. Connor began his employment with the Lone Star Group in 1921, and has been with it ever since. R. II, 861. Previously he had been employed to some extent to represent public authorities. But after his employment by Lone Star, he admits he changed his views materially about many matters pertaining to rate regulation, R. II, 1014-1015.

Mr. Connor's total estimated annual accruals were $3,465,123.36, (R. II, 1262; V, 3056) which would be equivalent to a 6% annual return on $57,752,-056.00. The Commission's allowance for depreciation and depletion (1931) on the 6% sinking fund basis was $983,698.43; R. I, 98, 107. This equals 2.13% of the Commission's rate base. The difference between the Commission's allowance and Connor's estimate is $2,481,424.93, which is equivalent to a 6% return on $41,357,082.00. Biddison and Steinberger found the overall percent condition of the property to be 94.26% (R. II, 1145) and the "observed depreciation"—which they erroneously used as being synonomous with "accrued depreciation" —to be 5.74%, as being the total accrued depreciation since the establishment of the Company in 1909. Biddison's testimony was that the replacements and

maintenance (the latter charged to operating expenses) were such as to keep the property stabilized in this high percent condition indefinitely, and that the property had not suffered any decline in percent condition over a period of the past 2½ years, R. II, 1142-1143, 1171, 1183; V, 3037. The unexpended balance in the depreciation reserve fund was shown to be $15,695,413.88 as of December 31, 1933, R. III, 2140B, 1657. If a proper relative balance had been maintained in the past between the actual accrued depreciation in the property and the unexpended balance in the reserve fund, theoretically this unexpended reserve of $15,000,000 plus should equal the accrued depreciation as found by the Company of 5.74%. (Upon this basis, according to the Company's computations, the property would have an undepreciated reproduction cost new of $273,439,-266.00!) Thus, the Company's estimated total accrued depreciation since 1909, of 5.74%, approximately equals the amount of annual depreciation as estimated by Connor.

It is also enlightening to compare Connor's estimates with the actual charges to the depreciation reserve in the past. (*St. Joseph Stockyards Co. vs. United States*, 298 U. S. 38, 65-67, 80 L. Ed. 1033, 1048-1049). The record shows that the average charges for the seven years 1927-1933 amounted to $344,871.84 per annum; and for the three years 1931-1933 amounted to $331,008.55 per annum, R. III, 2140B; V, 3363. These averages show that the charges are fairly uniform and are not increasing. This indicates with fair certainty that the property has now reached a stabilized condition where the ac-

tual current depreciation is fairly uniform from year to year and can be accurately measured by the actual charges to the depreciation reserves. This also accords with the testimony of Biddison to the effect that the properties are now maintaining a uniform percent condition, R. II, 1142-1143; 1171, 1183; V, 3037.

Despite the fact that the property is static insofar as decline in percent condition is concerned, and that the actual charges to the depreciation reserves are apparently uniform when averaged over a period of years, Mr. Connor found an annual depreciation allowance $3,120,251.52 in excess of the actual average annual charges to the depreciation reserves. (*Smith vs. Ill. Bell Tel. Co.*, 282 U. S. 133, 158-159, 75 L. Ed. 255, 268.) This is equal to a 6% return on $52,004,192.00.

Mr. Connor very candidly admitted that in making his estimates, he had given no consideration to the question of whether any, and how much, money had been or should have been collected from the rate payers in the past and set aside by the Company to offset depreciation as it accrued in the past, R. II, 1380-1392, 1433-1434; III, 2042-2043; V, 3061, 3083, 3094-3097, 3106-3114, 3116-3131. He insisted strenuously, however, that the effect of this method of approach was not to require the rate payers of the present and future to bear the cost of depreciation accruing in the past. (*Knoxville vs. Knoxville Water Company*, 212 U. S. 1, 13-14, 53 L. Ed. 371-380). The Commission laid clear emphasis upon this fatal error in Mr. Connor's calculations, in its findings, R. I, 78, 79, 85, 91.

The Company at pages 48, 153-154 of its brief complains that the Commission witness in his estimates of the amount of future accruals would have required the Company to use $5,000,000 out of its unexpended reserve balance of more than $15,000,000, for future removals, replacements and abandonments of property which had depreciated in the past. The record references show that Mr. Connor did not contemplate the use of a single penny of this reserve fund collected by the Company in the past for the express purpose of taking care of past accrued depreciation, simply because the removals, replacements and abandoments due in large part to such past accrued depreciation would not actually take place until the future, R. III, 2042-2043. Thus, Mr. Connor's estimates are not uniform over the entire life of the property, but depend upon the date of the rate inquiry; and he charges up in any rate investigation to the users of the present and future the entire cost of depreciation over the whole life of the property. The later the investigation, the greater would be his estimates. The estimates of the Commission's witness assumed the use of only such portions of the unexpended reserve as was determined to be necessary to offset this past accrued depreciation, and did not attempt to use any portion thereof which the Company may have collected from the past users in excess of its actual accrued depreciation. As an illustration of this point, the two large transmission lines B and C were installed in 1910. Substantial depreciation has accrued on these lines, and reserves have been or should have been, set aside in the past to offset this accrued depreciation. Under Mr. Connor's theory, no con-

sideration would be given to the reserves which should have been set aside in the past as this depreciation accrued, and the present and future rate payers would have to pay for the complete replacement, removal or retirement of these lines although the depreciation largely accrued in the service of past users.

In the state courts the Company made much capital of the claim that Mr. Connor's mortality curve equalled the actual mortalities of the past. This does not mean a thing. While on all other subjects Biddison and Connor protested emphatically that the past history of the Company was immaterial, paradoxically Mr. Connor at least purported to have made an exhaustive study of historical mortalities. But he did not correctly apply them in reaching his dollar results. It depends upon the shape of the assumed curve. The witness can shape the curve to serve his own purposes, and thus make the calculated past mortalities equal any given amount. The flatter the curve in the earlier years of the property (prior to a rate investigation), the steeper it must be in future years after a rate investigation. This is the principle upon which Mr. Connor would make the later users bear practically all the depreciation expense, although the Company undoubtedly has collected (as it should have done) at least the past depreciation from the past users.

The Company complains of the use of the sinking fund method of depreciation computations by the Commission and its witness. This Court has said, in *Clark's Ferry Bridge Co. vs. Public Service Commission of Pa.*, 291 U. S. 227, 240-241, 78 L. Ed. 767, 774, that, "In reviewing the findings of the state

court we are not required to enter a debatable field of fact and to choose and prescribe an invariable method of computation. To justify the overruling of the determination of the state court we must be able to see that what has been done will produce the result which the Constitution forbids. . . . We find it impossible to say, from a constitutional standpoint, that another method should have been employed or a greater amount allowed." In that case and in *Los Angeles G. & E. Corp., vs. R. R. Com. of California*, 289 U. S. 287, 295, 297, 298, 320-321, 77 L. Ed. 1180, where from the opinion it appears that the sinking fund method was used, such method has met the approval of this Court.

Furthermore, Mr. Connor himself, although using the straight line method on a few of his items, used the sinking fund method on most items, R. II, 1276, 1277, 1296, 1297, 1306-1316, 1321, 1322; V, 3056A, 3059, 3117, 3153-3157, 3161, 3178, 3179, 3185-3192. Mr. Connor used a 7% interest rate for sinking fund accruals in the hearing before the Railroad Commission, R. I, 80, 81; R, II, 1358, 1429. He used a 5% interest rate for sinking fund accruals in the District Court, R. II, 1262, 1276, 1277, 1296, 1297, 1306, 1310, 1315, 1316, 1321, 1322; V, 3117, 3161, 3178, 3179, 3182-3192. The use of a 5% interest accrual rate as used before the District Court increases the annual requirements over the amounts found under the 7% interest rate as used before the Railroad Commission. The Commission used a 6% sinking fund accrual basis, and the Commission's witness in the District Court used a 6% interest rate. The Commission also found that the sinking fund accrual rate

should be the same as the rate of return, R. I, 79-81; II, 1360, 1361; III, 1831 et seq., 1862, 1863. Both the straight line method and sinking fund method are generally recognized and would give the same results if properly applied, R. I, 77, 78; II, 1259, 1260; III, 1831, 1874-1875.

Typical of Mr. Connor's methods of inflating his estimates for both depreciation and depletion accruals, is his treatment of the withdrawals from gas reserves in estimating depletion. The history of the Company showed that up to the time of the District Court trial the Company's actual withdrawals from its own developed reserves were at the rate of approximately 5,000,000 to 6,000,000 MCF per year; R. I, 107 for 1927 to 1932 inclusive; R. III, 2124A, 2165, for 1933. Actual withdrawals by years were as follows:

1929	5,162,647 MCF
1930	6,473,463 "
1931	4,924,844 "
1932	4,829,077 "
1933	6,046,035 "

Instead of adopting the actual withdrawal rate, of from 5,000,000 to 6,000,000 MCF per annum being experienced by the Company, Mr. Connor assumed current and future withdrawals of 20,000,000 MCF, this being the same rate assumed by Dunn and Hulcy in capitalizing the value of gas reserves. He also based his unit depletion charge on the capitalized value of gas reserves found by Hulcy, which capitalization assumed a wellhead price of ($ .047) more than double the actual wellhead price ($ .020) for a

major portion of the Company's gas reserves, and of the unsoundness of which capitalization we will say more later. This method of computation resulted in an annual amount of $146,000 (20,000,000 MCF at $ .0073) and of $412,000 (20,000,000 MCF at $ .0206) as a part of the depletion and depreciation allowance on developed leaseholds and gas well equipment. If Mr. Connor had used the actual withdrawals being experienced by the Company, these particular inflated estimates would have been reduced by from two-thirds to three-fourths, R. I, 559, 560; II, 1266-1271, 1335-1337, 1348, 1349, 1352, 1353, 1364, 1365, 1456-1459; V, 3032, 3055, 3134, 3135, 3139, 3141, 3195, 3196.

If Mr. Connor was going to assume withdrawals of gas from Company reserves at the rate of 20,000,000 MCF per year as compared with the actual of 5,000,000 to 6,000,000 MCF in the past and at the time of the trial, he should either have assumed that gas purchases would have been accordingly reduced to the extent of the difference of approximately 14,000,000 to 15,000,000 MCF per year, which would have reduced the operating expenses approximately $900,000 per annum (see R. III, 2126D for average price of gas purchased), or, if he was going to assume that gas purchases would increase and keep pace with his assumed increased withdrawals from Company reserves, this necessarily would have quadrupled the Company's overall sales in the future, which would have resulted in quadrupling also its revenues. But Mr. Connor has not carried his assumptions to either of these logical conclusions.

Under no conditions should the Company have estimated its valuation of developed reserves, and its depreciation and depletion accruals, upon the assumed withdrawal of 20,000,000 MCF per year in the future, and at the same time based its operating revenues and expenses upon an entirely different basis.

As found by the Commission, a part or all of the depreciation on some items of property is currently charged to operating expenses as "maintenance," and all replacements and repairs to some items of property are currently charged to operating expenses, R. I, 75, 83, 84, 86, 87, 96, 97. With the exception of general tools, automotive and construction equipment and telephone equipment in part, Mr. Connor makes no deduction from depreciation for replacements being charged directly to operating expenses, R. II, 1353, 1354, 1374, 1375, 1429; V, 3055-3196.

As a further example of Mr. Connor's duplications, consider transmission line equipment. After fully allowing for all "future" annual accruals sufficient to provide for replacements due to physical condition of pipe; replacements, removals and abandonments due to operating conditions or public requirements; and major rehabilitations (R. II, 1281, 1282, 1298-1300; V, 3093, 3094, 3107), Mr. Connor makes a duplicate and additional allowance on transmission line equipment as well as all other items of property of 1% per annum for decline in per cent condition (R. II, 1271, 1276, 1277, 1305, 1306, 1315-1321, 1351, 1352; V, 3057-3196); and this despite Biddison's testimony (R. II, 1142-1143, 1171, 1183; V, 3037) that the property would not decline, and had not de-

clined, in per cent condition; and as a triplication he allows for the amortization of $17,970,000 of transmission line equipment to run concurrently with the 1% allowance for decline in per cent condition, R. II, 1262; 1321, 1322, 1431, 1434; V, 3056, 3056A, 3185-3192.

We have heretofore pointed out the fact that Mr. Connor's basic rates before adding these duplications and triplications were based upon making all future replacements, retirements, etc., without calling upon the reserves which should have been set aside in the past to take care of the depreciation which has accrued in the past.

Connor's total annual rate of 5.40% applicable to transmission line equipment included 3.54% for future replacements as taken from his base mortality curve, R. V, 3095, 3096. This primary curve was based upon a study of the mortalities from all causes in the Fort Worth distribution system; Mr. Connor having "assumed that the characteristics of the mortalities of steel pipe in service in the system of Lone Star Gas Company would rather definitely follow the general trend of the mortality curve previously developed for steel pipe in service in the system of Fort Worth Division—Lone Star Gas Company." A substantial portion of the items from which the Fort Worth mortality curve was developed grew out of inadequacy, public requirements, changed operating conditions and other factors distinct from the physical failure of the pipe itself, R. V, 3064, 3065. Although the 3.54% per annum allowance from the base curve included renewals due to inadequacy, public requirements and

changed operating conditions as reflected in the base curve from the Fort Worth distribution system experience, Mr. Connor allowed an additional .94% per annum for removals and abandonments due to changed operating conditions and public requirements, R. V. 3096-3098. (Also, see Railroad Commission findings, R. I, 88, 89). This duplication is additional to all of the duplications above pointed out with respect to the largest item of property, viz., transmission line equipment.

Moreover, in addition to meeting all of these duplicate future replacements, the total annual rate on transmission line equipment would build up a credit balance in the reserves as shown in Columns E, Tables V-A and IX-A, R. V, 3117, 3131; R. II, 1296-1297.

Even without any of the duplications and additions, Mr. Connor's base mortality rate as applied to steel pipe is excessive. A good test of the mortality rate can be had in the history of Lines B and C laid in 1910, the oldest lines in the transmission system, and lines with severe soil conditions. These two lines contain 646 miles of 3 inch equivalent pipe. The actual mortalities from all causes have amounted to a total of 9% of the pipe in 21 years. Mr. Connor's 25 year life base mortality curve would indicate a total of 25% of mortalities as compared with the actual of 9%. The 33½ year life base curve adopted by the Commission indicates calculated mortalities of 20% over the 21 year life of these lines, R. I, 89, 90; R. II, 1396-1401; R. III, 1837, 1838, 1854-1856. The obvious cause of Mr. Connor's high mortality rate can be traced to his use of the history of only 700 miles of 3 inch

equivalent pipe laid in Fort Worth during the period 1909 to 1931, over an area 10 to 12 miles square, where only 60% of the mortalities were caused by deterioration of the pipe, R. I, 88, 89; R. V, 3064-3065.

In the hearing before the Commission, Mr. Connor predicted 420,000 feet of 3 inch equivalent, of pipe mortalities, for 1932. The actual mortalities amounted to 27,374 feet of 3 inch equivalent diameter pipe, R. II, 1363, 1364. For a graphic comparison of the actual pipe mortalities compared with the pipe mortalities estimated by the Company witness, Connor, and as estimated by the Commission and its witness, see chart, R. III, 2182A. It is to be noted from the curve that the replacements for 1931 marked J and C are of the non-recurring type, R. III, 1842, 1863, 1864.

It is by means of such methods of computations and duplications pointed out above that Mr. Connor was able to reach the astounding total of $3,465,-123.36 per annum as his estimated depreciation and depletion allowance, this annual amount being approximately the same as the total accrued depreciation which has taken place in the properties since 1909 as estimated by other Company witnesses. Such methods and devious calculations have also permitted Mr. Connor to arrive at this annual estimate more than 10 times the actual charges to the depreciation reserves as being experienced by the Company.

An examination of the findings of the Commission and of Appellees' exhibits and testimony before the District Court will show that the depreciation allow-

ances made by the Commission are ample in every case to take care of all replacements, removals and retirements from every cause not being currently charged to operating expenses and will allow for the complete amortization of the entire property over its estimated life. The calculations are simple and straightforward and are in such detail as to show the adequacy of the specific allowances, R. I, 75-99, 107, 111; III, 1828-1843, 1851-1876, 2099-2102; 2158-2162D.

QUESTIONED OPERATING EXPENSES

We indicate in the following paragraphs the items, and the extent, to which we object to the operating expenses set up and claimed in the Company's various exhibits and computations. Even in our own Tables I to V inclusive, at the back of this brief, setting forth computations of the percentages of net return which would have been available under the 32c gate rate, we have not deducted any of these questioned items of operating expense except the Management Fees, and, in some of the Tables, certain of the "Donations" which were allowed, but held improper, by the Commission. This fact should be borne in mind by the Court in studying our Tables aforesaid.

The following figures are taken from exhibits based upon overall operations in Texas and Oklahoma, and are not segregated as between the two states:

Management Fees: Appellees' Exhibit 5, R. III, 2126A, shows that beginning with 1929, and extending to the close of the record before the District Court, the Company claimed as an operating expense man-

agement fees paid to Lone Star Gas Corporation averaging $91,040.32 per year for the five-year period 1929-1933. This amount would provide a 6% return on $1,517,339.00 in the rate base. Company witnesses attempted to justify this item only by outlining in very general terms certain "advice" and "services", "financial assistance", "purchasing services", etc., rendered to it by various persons connected with the holding company; and it made no attempt whatever to prove the actual or reasonable cost of these items to the holding company. Besides paying the holding company these management fees, the Company paid the full value thereof again, directly to the persons who rendered them, in the case of Haskins & Sells, Auditors, (R. I, 434); the salary of P. McDonald Biddison, engineer for the group (R. I, 416-417); the general counsel for the group, (R. I, 415); and paid the holding corporation 6% on all borrowings, made up principally of a $17,600,000.00 loan, R. I, 239-244. Obviously this is but a scheme by which the holding company milks the Company of its profits and at the same time attempts to camouflage as mere "advice" and "services" what in reality is absolute dictation. The Commission properly eliminated this item, R. I, 25-27. *Dayton P. & L. Co. vs. Railroad Commission of Ohio*, 292 U. S. 290, 78 L. Ed. 1267; *Smith vs. Ill. Bell Telephone Co.*, 282 U. S. 133, 152-157, 75 L. Ed. 255, 265-268; *Chicago & G. T. R. Co. vs. Wellman*, 143 U. S. 339, 346, 36 L. Ed. 176, 180; *Acker vs. United States*, 12 Fed. Suppl. 776, 779, affd. 298 U. S. 246, 80 L. Ed. 1257; *Western Distributing Co. vs. Public Service Com.*, 285 U. S. 119, 126-127, 76 L. Ed. 655, 659;

United Fuel Gas Company vs. Railroad Commission of Ky., 278 U. S. 300, 320, 73 L. Ed. 390, 401.

Donations: The Commission (R. I, 23) included as allowable, under the title "Miscellaneous General Administrative Expense, $49,012.06" for 1931, the "charitable donations" which (R. III, 2228) averaged $10,284.05 per year for the three years 1931-1933. This item alone would have provided a 6% net annual return on $171,400.00 in the rate base. The Commission found, however, that "donations are not proper future operating charges. For the time being we are computing the actual 1931 expenses including charitable donations ($9,848.67) and the subscriptions and donations ($20,215.94) included in miscellaneous general administrative expense. This fact should be given its due weight in the consideration of 1931 rate of return," R. I, 23. The $20,215.94 "subscriptions and donations" would have provided a 6% return of $336,932.00 additional in the rate base.

There is no break-down accessible in the record by which we can determine how much of this amount was "donations" which we question, and how much was "subscriptions," which we do not question. As to all donations, charitable and non-charitable, however, we contend that they are not permissible operating expenses. *Idaho Power Co. vs. Thompson*, 19 Fed. (2d) 547, 548; *McCrory vs. Chambers*, 48 Ill. App. 445; *Holt vs. Winfield Bank*, 25 Fed. 812; *Davis vs. Old Colony R. Company*, 131 Mass. 258, 41 *American Reports* 221. A public utility must confine its expenditures to such as are legitimate for carry-

ing on its business. It may not, as between itself and the public, take the same liberties that a corporation may assume as between itself and its stockholders. Even in the latter case, donations, though calculated to advance the interests of a corporation, are not permissible over objections of the stockholders, and certainly are not permissible as against the public in a rate case.

Uncollectible Bills: Commission accountant Phillips, Exhibits 5, III, 2126A, shows "bad debts and adjustments" averaging $3,632.29 for seven years 1927-1933. This would provide a 6% return on $60,538.00 in the rate base.

Article 1440, R. C. S. Texas, 1925, provides "Deposits for installing service. Every . . . corporation . . . engaged in the furnishing of . . . gas . . . which requires the payment on the part of the user of such service of a deposit of money as a condition precedent to furnishing the same, shall pay 6% interest per annum on such deposit to the one making the same . . .".

This is a statutory recognition of the right of public utilities, such as Appellant, to require the deposit of a sufficient amount in advance from the customer, before the services are rendered, to indemify against the incursion of bad debts. *Central P. & L. Co. vs. Purvis*, 67 S. W. (2d) 1086, 1089.

This being true, we do not think bad debts are a proper charge against operating expense in public service operations. At R. I, 331, Hulcy explains these by saying "well, that is just some bills that we

did not collect.' We failed to get our money from the sales of gas." And at R. I, 437, he states that these bills are not owed by the affiliated companies but by private consumers along the rights of way. The Commission (R. I, 29-30) allowed the inclusion of this item at $7,727.33 for the year 1931, which was far above the average for the seven year period above shown, and would have provided a net return of 6% on $128,789.00 in the rate base. We think this item of expense should be eliminated from all computations of rates of actual return hereinafter.

Regulatory Commission Expenses: The Commission (R. I, 22-23) allowed $17,695.86 for the basic year 1931. The Commission found that necessary expenditures of this character in reasonable amounts "are properly chargeable to this account. Any expenditures for valuations, expert witnesses, or other items in defense of rates sought to be maintained by the Company, which expenditure is in excess of a reasonable amount should be borne by the owners of the Company. The 1931 regulatory expense was not relatively large. Whenever such expense is relatively large (such as 1932) it should be amortized over a reasonable length of time, say ten years. The instant case is the first time since the incorporation of the Lone Star Gas Company in 1909 that the Company has had occasion to incur any regulatory expense by reason of a hearing before a Texas Regulatory Commission." R. III, 2131, 2228 shows this item in the amount of $163,739.01 for 1932, and $66,792.39 for 1933. According to the Commission's findings these large amounts for 1932 and 1933 should be amortized respectively over periods of 10 years, which

neither the Company's accountants nor the Commission's accountants have done in the preparation of their operating statements except in the case of Company Exhibit 13. This should be done in the computations of rates of actual return on the question of confiscation.

Dry Hole Expense: The Commission (R. I, 28-30) allowed this item in the annual sum of $79,453.12, upon the basis of an average for the five year period 1927-1931. From R. III, 2126A, it appears that this item, as charged on the books, amounts to an annual average of $61,465.52 for the seven year period 1927-1933. The Commission pointed out (R. I, 28) that this item was computed upon the basis of an actual five year average and that this item was "in the nature of money advanced for the development of gas which will be produced in future years . . . . . the Company should be precluded from capitalizing dry hole expense in any future rate investigation."

The average allowed by the Commission was substantially in excess of the actual average for the seven year period, and if the production system properties be included in the rate base, and production expenses in the operating account, certainly the allowance is more than sufficiently liberal.

Of course, the doubtful question of whether these production system expenses (both dry hole expense and cancelled and surrendered leases, next discussed) should be included in the operating expense account at all, is tied in directly with the very doubtful ques-

tion of whether all of Appellant's production system properties should be included in the rate base (which we shall discuss later), or whether it would not be more just to pursue the method adopted by Commission witness Freese in his testimony and exhibits before the District Court, of excluding both production properties from the rate base, and production expenses from the operating account, and substituting in lieu thereof the allowance of the actual average prevailing field price being paid for gas purchased in Texas, R. III, 1795-1796, 2098-2099, 2164. The Commission several times in its opinion referred with approval to the appropriateness of applying the well head price in evaluating Company-produced gas, though in the end it did not adopt that method, R. I, 19, 20, 67-74, 104, 105, 113, 114.

Cancelled and Surrendered Leases: Much that we have said under "dry hole expense", above, is applicable here. The Commission (R. I, 28-30) discussed this item (cancelled and surrendered leases) fully and allowed $99,140.73 per annum. Reference R. III, 2126A, will reveal that the average charges to this account were relatively small up to the end of 1930. During 1931 increased funds were appropriated by the Texas Legislature for the use of the Commission in investigating natural gas pipe line rates, and the experts who testified for the Commission in this case, both in Commission and court hearings, were employed in that year, R. III, 1796. This is the only reasonable explanation of the fact that the cancelled and surrendered lease charges (R. III, 2126A) jumped to $239,230.96 for 1931, $255,829.03 for 1932, and $188,629.92 for 1933. Obviously these exorbitant and greatly in-

creased charges, incurred in unsuccessful exploration of Company-owned undeveloped leaseholds, were charged into the expense account with a view of an approaching rate investigation.

This is even more obvious when the leasehold account (gas leases, rights and lands in fee) is examined. It is to be noted that this capital account increased steadily in the approximate annual amount of $300,000, from January 1st, 1927, to December 31st, 1930, and then decreased steadily during 1931, 1932 and 1933, R. III, 2140A, 2211, 2214, 2217. Cancelled and surrendered lease expense is not an "out of pocket" expense during the accounting period in which the leases are charged off, but is simply a book transfer from capital account to operating expenses of the cost of leases acquired and capitalized in previous accounting periods. These book transfers are made at the will of the management. There is nothing in the record to substantiate the reasonableness of these charges during 1931-1933, inclusive. Although the Commission has allowed in the rate base, on which the 32c rate was fixed, the cost of undeveloped leaseholds, including delay rentals, as of December 31, 1931, and has allowed as operating expenses cancelled and surrendered leaseholds, it is obviously to the advantage of the Company to obtain the benefit of taking from gross revenues these huge operating expense charges, each dollar of which absorbs the equivalent of a 6% net annual return on $16.67 in the rate base. In other words, the charges for 1931 would absorb the return on $3,987,183.00; for 1932 the return on $4,263,817.00; and for 1933 the return on $3,143,832.00.

Inasmuch as all of the Company's production system properties as of December 31, 1931, including costs of undeveloped leaseholds and delay rentals, were included by the Commission in the rate base upon which the 32c gate rate was fixed, the following is a true picture of what has been happening ever since the end of 1931: with the gate rate remaining static and unchanged since the end of 1931 and with the production system property account actually declining (R. III, 2140A, 2211, 2214, 2217), at the same time the Company has been attacking the 32c rate upon the basis of rapidly mounting operating charges in the form of cancelled and surrendered leases, each dollar in such operating expense account being the equivalent of $16.67 in the capital account, or rate base as pointed out above. Thus, the consumer is caught in an enfilade of devastating fire from both directions.

New Business Expenses: For 1931, the basic year used by the Commission for fixing the rate, these items totalled $126,125.98,—broken down as follows:

New business advertising salaries $9,548.77;
New business soliciting and commissions $27,969.98;
Advertising supplies and expenses $81,234.85;
New business supplies and expenses $7,372.38.
(R. I, 30)

The Commission allowed, without question, all of the above items, except the $81,234.85 for advertising supplies and expenses, R. I, 22. It pointed out that this latter item was subject to numerous objections, but reluctantly allowed it in full because it was not clearly shown that all of it was subject to the objec-

tions pointed out, and there was no evidence submitted which would enable the Commission to segregate the proper from the improper portions, R. I, 23-25, 30. This item ($126,125.98) is clearly excessive and unreasonable upon its face. It absorbs a 6% net return for 1931 on $2,102,100.00. This is the basis on which operating expenses for the future were allowed. Smaller, but still grossly excessive, amounts were charged for subsequent years (R. III, 2227) as follows:

1932 $87,528.94 which equals 6 per cent return on $1,458,816.00.
1933 $99,793.94 which equals 6 per cent return on $1,663,232.00.

It is to be recalled that the bulk of the Company's business consists of gate sales only, to its affiliated distributing companies, the acquisition of whose business occasions no expense whatever; and of very small sales to independent distributing companies at Gainesville and Waxahachie, who are shown already to be under long term contracts which, so far as the record shows, cost the Company nothing to acquire (R. IV, 2323, 2342); and to approximately 90 industrial customers, along its rights of way, listed in the portion of the record which has been printed, (R. IV, 2386-2590) and to such farm taps as are served along the rights of way, R. I, 407.

Hulcy testified that this expense includes cost of soliciting business, and advertisements in newspapers and trade magazines; and that its purpose is to attach customers to the *distribution companies served*, and not to attach new customers to its pipe line business

except insofar as industrial business is obtained through solicitation and commissions; that its purpose is to increase gas sales by acquainting the customers with the advantages of gas as a fuel, R. I, 406-408. He could not state how much of the expense, if any, was incurred for advertising directly aimed toward increasing the use of gas and pointing out to gas customers the more extensive uses of gas and new gas appliances, R. I, 410.

The Company did not produce any evidence as to the value or cost of the newspaper advertising, nor give any evidence of the nature and contents of same, aside from what has been stated in substance above, either before the Commission or the court. As shown by the Commission's criticism, however, (R. I, 23-25), at least some of this advertising was pure political propaganda, to the effect that "60c of every gas bill goes for taxes."

Furthermore, everyone acquainted with the contents of modern newspapers, and with the habits of people living in modern urban centers, knows that no gas customer has ever been attached, or retained, through the medium of newspaper advertising, but that the prospective customers are all well acquainted with the merits of gas, and use it of their own accord, if they can afford it, in preference to all other fuels without any newspaper advertising.

If the Company had produced evidence before the Commission or court which would disclose how much of this large item of expense was legitimate advertis-

ing, we would have had no objection to the allowance of a reasonable amount therefor. But we do object strenuously to the inclusion of an unreasonable sum, of approximately $100,000.00 per year, which is shown affirmatively to be in part tainted by impropriety. And we think because of the Company's failue to adduce the required proof, the whole item should be stricken in determining confiscation.

All this is aside from the view expressed by Mr. Justice Stone that new business expense is not a proper charge against the present users: *West Ohio Gas Co. vs. Pub. Ut. Com.* (Lima case) 294 U. S. 62, 77-78, 79 L. Ed. 761.

Federal Income Taxes: An examination of the Company's exhibits analyzing its actual operating expense, will disclose that no federal income tax is included; which means, as is admitted by Hulcy, that the Company has never paid any, R. I, 405; R. III, 2224-2228. The Company, up through 1933, made consolidated income tax returns with its affiliates for the whole group, and the amount of tax paid thereon in such years (if any tax has actually been paid at all) was paid by the holding company, Lone Star Gas Corporation. The Company adduced no evidence as to how much income tax, if any, had been paid by the holding company, R. I, 399. The amount of taxes as between the holding company and the government was in controversy, and had never been settled. Nevertheless, it is shown by the record that the Company each year made out a "dummy," or memorandum income tax return, on the basis that would have been used had it made a separate return of its own to the

government, and this dummy memorandum return was passed on to Lone Star Gas Corporation, and not to the government, R. I, 396, 397. (Hulcy when asked on cross examination concerning this return evaded the question and testified "You are asking about something filed with the Federal Government, and which is entirely beyond our control", R. I. 602). The Corporation then would bill back to Appellant certain purportedly allocated amounts, the basis and correctness of which claimed allocations are not shown in the record. The Company would then credit the Corporation with the amount so billed, but even these amounts (aside from the question of their correctness) are not shown, with the exception of $296,954.64 for 1931 and $234,312.46 for 1932, R. I, 395.

We submit that this evidence is totally insufficient on which to establish any real and reliable allowance for Federal Income Taxes actually incurred or paid. The Commission found (R. I, 104) that "throughout this opinion we have computed return before Federal Income Tax." This means that its intention was to fix an average annual net return of 6 per cent before, and without deduction of, Federal Income Tax as an operating expense. It further found (R. I, 104-105) that after taking credit for depreciation at the rate allowed by the Internal Revenue Department and for interest on borrowings as permitted by the Department, there would be no liability for a federal income tax upon the basis of a 6% return in the future. Nevertheless, Hulcy, in making his computations of amounts available for net return, deducts computed amounts for this item in the grossly excessive

sums of $302,302.41 for 1931 (R. III, 2210), and $343,835.27 for 1932 (R. III, 2213).

The method by which he arrived at these computed, as distinguished from actual, income taxes is that in some instances he failed to take credit for interest on borrowings as permitted by the Internal Revenue Department, the principal item of which was made up of 6% paid the holding company on indebtedness ranging from $19,000,000.00 at the peak to $17,600,000.00 at the time of the District Court trial, R. I, 464; and, in some of his exhibits, instead of taking credit for the 5% depreciation actually allowed by the Internal Revenue Department in the past, he deducted only the amount, (2% plus), of depreciation as allowed by the Commission in its opinion, R. I, 405, 406; R. III, 2287.

Cross examination by counsel for the State developed from Hulcy that in Company Exhibit 13, (being the analysis of the comparative statement of revenues and expenses based on 32c domestic gate rate using rate base as found by Commission at December 31, 1931, plus net additions at cost) that if the depreciation be deducted in the amount of 5% which was the amount allowed by the Internal Revenue Department before calculating federal income tax, that the resulting federal income tax would have been approximately $52,000, plus, instead of the amount of $211,689.58, which is shown in the exhibit, R. I, 405-406; R. III, 2287, 2296.

In view of the fact that the Commission found that the 6% return fixed would be reasonable, without deduction for federal income tax; and that if proper

credit were taken for interest on borrowings no federal income tax would be due on a 6% basis (R. I, 104, 105); and in view of the Company's failure to produce any evidence of how much its actual income tax had been or would be, we do not think it would be justifiable to deduct in computations of net return for confiscation purposes any sum for federal income taxes.

RATE BASE

Quoted Prices: By far the largest item of physical properties was transmission line equipment, which was estimated by the Company, (R. V, 3038) in the amount of $31,894,439.40 of which amount pipe delivered at the sidings amounted to $20,954,471.01, R. V, 3052. As the basis of obtaining prices on pipe, as well as practically all other items of physical equipment, the Company purported to have obtained from "leading manufacturers" quotations of the prevailing prices, with all applicable discounts applied.

It was obvious that the Company's inquiries asking for quotations on the quantities of materials contained in the entire system were not made with a view of actual purchases of any such quantities, and the manufacturers were therefore bound to have known that the quotations were requested for rate evaluation purposes. The competition motive for quoting the lowest prices and the greatest obtainable discounts, to obtain an actual order in such vast quantities, was therefore totally lacking; and the manufacturer would, of course, not wish to offend actual customers of the past or prospective customers of the

future by quoting in those circumstances the lowest prices for such quantities available in case of a real purchase. Biddison testified (R. I, 648) that he believed in case of an actual purchase the pipe might be bought at prices "slightly under" the quoted prices, but that he was of the opinion, also, that the placing of orders in such large quantities would so stimulate the prices that they would not hold very long if that amount of business became available to the manufacturers. He stated, further, that in the placing of orders, for *actual* purchase of pipe, there are opportunities to "chisel a little", on the prices to be paid, but that he had not taken that fact into consideration in the preparation of his appraisal, R. II, 810. He attempted to deny that discounts of certain percentages were available on large lot pipe purchases, in the face of two telegrams from the manufacturer that they were so available, R. I, 657, 660, 685-686.

The Company avails itself of the services of J. M. Simpson, who maintains his office in Pittsburgh, Pa., and acts as common purchasing agent for all pipe and heavy materials for the entire Lone Star group as well as for other large groups of utility purchasers; and it was upon the theory that Simpson was able to obtain for the Lone Star group the lowest prices available to any purchaser on large or small lots that the Company attempted to justify in part its payment of management fees to the holding company, R. II, 905; R. III, 1980-1983. When it came to obtaining prices for evaluation purposes, however, it appears that the services of Mr. Simpson as purchasing agent were utterly worthless. The Company did not call Mr. Simpson as a witness to substantiate its prices as applied.

A striking example of the inflation injected into these prices is found at R. II, 902-904, where it is shown that during 1933, immediately after the date of Biddison's appraisal, the Company had actually made substantial purchases (11 carloads in one instance) of the highest quality large size pipe at prices very substantially lower than Biddison used in estimating the prices of lower quality smaller size pipe.

The Commission's witness, Freese, testified that his investigation showed that large lot purchases could be obtained at prices 10% to 15% or more below quoted prices, R. III, 1746-1747, 2096-2097. The Commission's opinion (R. I, 37-40) discloses that quoted prices from the leading manufacturers were identical and far above the prices actually obtained by the Company in actual purchases.

The Company sponsored an exhibit purporting to show a total increase in price of steel pipe in its system of $1,105,652.54 between January 1, 1933, and the last appraisal in 1934, R. V, 3052.

It conclusively appears that this temporary rise was due to the artificial inflation of the "steel code" (August 29, 1933, R. II, 900) under the National Industrial Recovery Act, which became effective prior to the latest Company appraisals, R. I, 420; R. II, 771, 901, 1229-1230; R. III, 1763, 1982. The same artificial stimulus was responsible for the Company's increase of common labor rates from 35c to 40c per hour, R. III, 1618, 1722. The NRA has long since been declared unconstitutional and the artificial stimulation has subsided.

Company witness Schmidt attempted to explain the Company's actual purchase of 24 inch pipe in 1933 at approximately $2.00 per foot, when the quoted price of $3.00, as used in the appraisal, by saying it was a "distress purchase," R. III, 2045-2046, 2051.

We have given in some detail the inflation resulting from the use by Appellant's witnesses of quoted prices rather than the use of prices at which the Company was actually purchasing the material. Throughout the appraisal Biddison, practically without exception, has used quoted prices; and, in fact, he seems proud of the fact that he had made no search of the Company's records to ascertain at what prices materials were currently, or within a recent period of time, being purchased by the Company: Gas Wells, R. I, 618, 624, 626; Other Production System Structures, R. I, 632, 633; Welding, R. I, 743; Lumber and Gravel, R. I, 751, 757. There are many other instances throughout the record.

Biddison, even though using quoted prices and discounts as furnished by manufacturers, without relation to actual purchases by the Company, failed to apply all of the discounts applicable even to such quotations, as for instance, in the purchase of casing where the record clearly reflects that the current quotation was 10, 10 and 2 from list, whereas the witness Biddison used a discount of 10, 5 and 2 from list, R. I, 657-659, 685-686.

Divided Responsibility: A single illustration of the substantial and inevitable error which results from the divided responsibility of having one witness responsible for prices, another for inventory, another for

application of unit prices, another for cost studies, another for the interpretation of the analysis of cost studies, another for the estimates of volumes of gas reserves, another for evaluation of gas reserves, another for evaluation of intangible elements, etc. *ad infinitum*, as per the division of labor between the expert witnesses used by the Company, is the following: That Biddison, in evaluating gas well equipment, included a large lot of miscellaneous special manufactured valves, and applied his idea of "substituted" quoted prices to same; resulting in the application of prices in some instances of more than $700.00 on valves which should properly have been priced at around $200.00; and Biddison was finally compelled to admit that because of the error in this particular instance his appraisal should be reduced to the extent of $4,603.78, R. II, 1171.

Another typical example is that Biddison, after being smoked out in cross-examination made a re-check and eliminated $25,473.00 for well lines which should have been excluded from the appraisal. Biddison had no part in the preparation of the inventory. He had no part in the determination of the prices for materials used in the appraisal, and was surprised to learn that included in the inventory were well lines and wells which were no longer used and useful in the public service, R. I, 746, 747; R. II, 1141.

Furthermore, this method lends itself admirably to the game of "passing the buck." Whenever a witness was pursued too closely on cross examination he could always find a refuge of safety by saying that he had no responsibility, that this matter was handled by some other witness, and thus the whole method

provided a wonderful opportunity to the Company of covering up numerous and substantial errors and duplications in the work of the witnesses; and which the Commission was, of course, utterly unable to discover and expose, in cross examination, except in isolated instances where the witnesses could not elude confession of error, R. I, 657-659, 685-686.

Excavation Costs: The total yardage of excavation estimated by the Company was 3,375,162.9 cubic yards, R. II, 1255. Of this total yardage, 2,786,080.03 cu. yds. or 82.54% were estimated as to volume, and classified as machine, rock and hand earth excavation, by what is known as the "barring method". That is, instead of making an opening over the pipe, a steel bar is driven into the ground until it contacts what is supposed to be the pipe, and in this way the depth of trench cover is measured; the outside diameter of the pipe, plus a few inches additional for "bedding" where it is concluded that rock excavation was done, was added to the trench cover, and the total trench depth thus determined. Trench widths could in no instance be ascertained except where actual construction records were available, which was the situation on only a very small part of Appellant's system. Thus over most of the system, trench widths had to be estimated, and the total yardage of estimated excavation thus determined. The Company operatives would then again drive the bar into the ground a few feet to the side of the pipe to determine whether there was rock. If the bar struck rock at any depth it was assumed that the soil from that depth downward was all rock, although it might have been only a thin ledge, R. I, 489-490, 497-498, 500-502; III, 1618.

A striking concrete example of the utter unreliability of this method is afforded by a comparison of actual construction records on Line Second B and the results obtained by barring methods on Line B, with the two lines running parallel 60 or 70 feet apart for a distance of 62.12 miles (R. II, 1256). Line B was constructed about 1910, and no actual records were available; consequently the barring method was used on it. Line Second B was constructed in 1929, and actual construction records were available. Cross-examination of Steinberger discloses that the barring method used on Line B produced an estimate of 11.97% hand earth excavation, 11.11% of hand rock excavation, and 76.92% machine. At the same time the actual records revealed that on Line Second B the percentages were: hand earth excavation, .83%, hand rock excavation 9.07%, and machine excavation 90.10%. In other words, the hand earth excavation estimated on Line B was 14.42 times as great as the hand earth excavation actually encountered on Line Second B, and the hand rock estimated on Line B was materially greater than that actually encountered on Line Second B; R. I, 501-504; R. II, 1249-1256.

Steinberger had assembled the detailed underlying data for purported cost analyses or studies of actual excavation cost on approximately 452 miles of trenching done on the system after 1929, no actual records prior to that year being available, R. I, 497-498. Steinberger, from this immense mass of detailed data, compiled his own "summaries" or "conclusions", as to what he interpreted the detailed data to show in the way of unit costs for the various classes of excava-

tion. He then passed these "summaries", or "interpretations", or "conclusions" of the data to Biddison, who, though admittedly knowing nothing of the detailed data or conditions under which the work had actually been performed, made "modifications" of Steinberger's "summaries, conclusions or interpretations", to suit his (Biddison's) own ideas of how the data ought to be rectified to apply in the present reproduction cost estimate because of supposed differences between conditions under which the work studied was actually performed (and of which conditions Biddison admittedly had no knowledge) and the hypothetically different conditions under which the property would be reproduced. This again presents an ideal opportunity for "padding" the hypothetical, as distinguished from actual, cost, and for making the most of the Company's preconcerted plan of dividing responsibilities so that no one could effectively be called to account for the unrealities and errors.

The Company witnesses used four classifications of excavation, which in direct order of cost were: (1) machine, $.4260 per cubic yard, (Line K) R. II, 779. The unit cost per cubic yard for machine excavation used by Biddison varied with the width and depth of the trenches—the unit costs ranging from about 40 cents to 45 cents per cubic yard, R. II, 785; (2) hand earth, in stretches more than 200 feet in length, $1.31, per cubic yard, R. II, 779; (3) hand earth excavation on "skips" or "lifts" of less 200 feet in length, encountered in connection with machine excavation, $2.138, (R. II, 1219, 1223); and (4) rock excavation, in Texas $3.897 per cubic yard, and in Oklahoma, $3.826 per cubic yard, R. II, 784; III, 1924.

These unit costs the Company purported to have derived from its aforesaid studies of actual construction costs, with the exception of unit costs for hand earth excavation on stretches in excess of 200 feet in length, which price of $1.31 per cubic yard was developed by witness Biddison through the device of a hypothetical gang set-up, Biddison admitting that no Company cost records were available on hand earth excavation on stretches in excess of 200 feet, R. I, 640; R. II, 784.

The absence of these actual cost records is sufficient proof that the Company had not actually encountered hand earth excavations on stretches in excess of 200 feet in its actual construction study. An examination of Appellee's Exhibit 6 (R. III, 2151) reveals substantial estimated amounts of hand excavation on certain stretches, as for example, 15,621.3 cubic yards of hand excavation in the "C" system, which together with machine excavation of 45,910 cubic yards and rock excavation of 1,405.5 cubic yards, constitutes the yardage in the "C" system. Other similar illustrations are shown at R. III, 2151-2152. It is to be noted classifications and quantities of excavation were furnished Appellees by the Appellant, R. I, 874. This yardage of hand earth excavation was classified by the Company, based primarily on the barring (estimated) method, but also includes those lines on which actual records of the construction were kept, R. I, 497, 498, 502, 505; R. III, 1923-1924.

The Company's methods resulted in gross and obvious overestimation of the yardage of hand earth excavation of both classes, and of rock excavation, with an underestimation of machine excavation yardage, and the application of the higher price of $2.138

per cubic yard to a large portion of the estimated hand excavation, R. II, 779.

Although the records show there were many field and tap lines in the system, ranging up to as much as 7 miles in length, (R. I, 722, 724), Biddison assumed hand earth excavation on these field and tap lines almost without exception; giving as his only reason therefor that it would be more expensive to move a machine in on the job than to do it by hand—yet, on his assumption of 100% reproduction new, the machines would be available on the main line trenches for use on the field and tap lines as they were reached, R. I, 501. These tap lines are the main line taps or laterals extending to city gates and industrial connections.

Next to the $21,000,000.00, cost of pipe, the cost of excavation was the largest other item in making up the total of approximately $31,000,000.00 for transmission line equipment, as estimated by the Company, R. II, 763-764; R. IV, 2365; R. V, 3052.

Furthermore, Biddison and Steinberger included in their unit cost of machine excavation their cost of "crumming", or cleaning up in the ditch following the machine. In several instances, cross-examination succeeded in establishing that they had included in the supposed work of these "crumming" or clean-up crews, the cost of quantities of rock excavation, which of course, was much more expensive and should not have been thrown into the machine costs.

Steinberger testified from his daily progress reports, which reports furnished the basis for his studies of excavation, as follows:

"Q. Go ahead.

A. I have a day here, Oct. 29th. We have 671 labor hours working from stake 386-00 to 476-00, a distance of 9000 feet charged to "crumming," crumming ditch and removing rock.

Q. Well, that is part of your hand excavation cost?

A. No, it is not.

Q. What have you figured that in,—as a part of the machine excavation?

A. Yes, crumming is part of machine excavation, just like clearing off a ditch is part of it" R. III, 1946.

A similar illustration of the opportunity afforded for "padding" the unit costs derived from a study based upon the daily progress reports can be cited as follows: witness Steinberger in testifying from daily progress reports of August 28th:

"Q. Wasn't there any crumming behind the machine?

A. Apparently not. Whatever crumming there was, was included with rock excavation. . . .

Q. So that to the extent you have left crumming out in the rock excavation you have understated the performance actually done by the rock excavation gang?

A. That is correct. One day it may be understated on performance and other days, overstated," R. III, 1944, 1945.

Freese compared the relative percentages of the various classes of excavation as determined by the barring method on Line B with the actually experienced relative percentages of excavation on Line Second

B, Line Second B being some 60 or 75 feet from and parallel to Line B, R. I, 503; II, 1251. Freese testified that if the Company had determined the classifications of the yardage by actual measurements and had applied the unit costs used by Biddison to the yardage so determined instead of the classifications as used by Biddison, that the cost of the excavation as shown in the Company's exhibits would have been reduced in the approximate amount of $600,000.00, R. III, 1779-1780.

Freese applied the following unit prices to the various classes of excavation: machine, $.375 per cubic yard; hand earth, $1.31; rock, $3.50, R. III, 1744. The Appellee also used as witnesses, Robinson and Dobson. Robinson was a contractor residing in San Antonio, Texas, who had done much excavation work in the area traversed by the Company's transmission lines, R. III, 1610. Dobson was undoubtedly the best qualified witness on machine excavation that appeared in this trial. His qualifications are shown at R. III, 1710. He testified that he now owns and operates 30 trenching machines. He also testified that, using only his own equipment, he could trench the Company's system in two seasons of 8 months each, R. III, 1720-1721. Robinson and Dobson were carried over the system and were given specifications describing the manner in which the trenching or excavation had been classified and the classification in cubic yards of rock, hand earth, and machine excavation, R. III, 1712-1721.

It will be noted that Freese, as well as Robinson and Dobson, had 3 classifications—machine, hand earth,

and hand rock. All three testified that it was customary for such hand excavation as is incident to the machine excavation to be included in the unit prices for machine excavation, R. III, 1616, 1719. Dobson testified as follows: estimated machine excavation, $.285 per cubic yard; hand excavation $1.41 per cubic yard; rock excavation $4.00 per cubic yard, R. III, 1721-1722. Robinson testified: machine excavation 40c per cubic yard; hand excavation, $1.20; rock excavation, $2.90, R. III, 1617. Robinson and Dobson would have been glad to do the work at the prices testified to by them, R. III, 1723, 1624. Freese relied not only upon his own independent judgment as to the proper prices to be used for the various classifications (R. III, 1773-1774), but also upon the testimony of Dobson and Robinson.

A similar controversy as to excavation costs arose before the Commission. There will be found in the findings of the Commission detailed discussion of the testimony relative to this item before the Commission, the State having introduced in evidence before the Commission the testimony of Lee, Minter and Sherman in addition to Robinson and Dobson. The testimony of Lee, Minter and Sherman before the Commission confirmed the testimony of Robinson and Dobson. The Commission used substantially the highest figure on each classification testified to by any of Appellees' witnesses, R. I, 42-43.

Freese adopted the estimates of the Company witnesses as to backfill. There is no dispute as to this item, R. III, 1772.

Freese testified that he had examined the studies made by the Company on excavation, both on trans-

mission lines and on well or field lines. He testified that it would be improper to use unit costs developed by studies on actual measured excavation when applied to quantities determined by the barring method, R. III, 1779-1780. He further cited as an illustration the comparison between Line Second B, the measurements of actual construction of which were available, and the quantities on Line B, which were determined by the barring method, R. III, 1779-1780; the results of which comparison are stated above. Freese also cited studies of excavations on field lines in the Texas Panhandle and Oklahoma gas fields. These studies were made by Steinberger. Freese testified as follows: "Certain information was made available to us. However, it was not in such shape as we could analyze it and make heads or tails of it. I think that is apparent in this particular case. When you analyze in the Panhandle field, according to the Company's records you show a cost of rock and earth excavation of less than a dollar; in Oklahoma of around 60c or 70c on field lines; then when you analyze what is set forth in connection with machine excavation it runs up to over $2.00," R. III, 1771. In State Exhibit 6, R. III, 2151, 2152, is shown in tabular form the excavation yardage, unit prices, and amounts in dollars as used by Freese. The total allowance for excavation as estimated by him is $2,221,059.90, R. III, 2151, 2152. Steinberger testified that, on this item of excavation, Biddison had included in Company Exhibit 28, $558,008.58 more than the amount estimated by Freese in Exhibit 6, R. III, 1955.

Gas Reserves: Before the Commission and the District Court, the Company included in its appraisals

all developed and undeveloped gas reserves and leaseholds owned by it. The Company's statement to the contrary on p. 36 of its brief is absolutely unfounded. Freese's exhibits before the Commission, likewise included these reserves. The Commission included in the rate base all of the production system properties both in Texas and Oklahoma, except Petrolia (Texas) field, where the cost of operation alone was so grossly in excess of the worth of the gas that the Commission determined it would not be proper to allow these worthless production properties in the rate base as used and useful public service property, R. I, 47.

The record showed that in the past the Company had been producing only approximately 28% of its over-all deliveries and had been purchasing approximately 72%, R. I, 72. Freese testified, before the court, that 80% was purchased, and 20% produced, R. III, 1894.

According to the Company's evidence the average field price being paid by it for purchased gas over-all in Texas and Oklahoma, even giving effect to the much higher prices prevailing in Oklahoma, was only slightly in excess of 6c per MCF, R. I, 606-607. The average prevailing field price in the fields where the Company produced gas was slightly less than 5c (4.82c for 4, 924,844 MCF, or $237,233.40 for year 1931, R. I, 107, 113). In Texas it would be slightly less than 4c. (3.90c to 3.96c, R. III, 2165).

But if effect were given to the Company's methods and estimates, all the gas produced by it would cost 23.3c per MCF *at the well head*. The Company esti-

mated depletion of developed leaseholds at $146,000 per annum (R. V, 3055); depletion-depreciation of gas well equipment at $421,316 per annum (R. V, 3055); production system expenses amounted to $105,554.86 for 1933 (R. III, 2224); cancelled and surrendered lease expenses amounted to $188,-629.92 (R. III, 2215); production system property was included in the Company's proposed rate base at $9,108,352.94; not including non-physical values, (R. V, 3037), which at 6% return amounts to $546,501.18 per annum. This makes a total of $1,408,001.96 for the 6,046,035 M C F of Company-produced gas for 1933 (R. III, 2124A, 2165) or 23.3c per MCF at the well head.

It is not amiss to remind the Court that the Company and the Commission included in the rate base all production system properties, when plainly a very large part thereof (all of the so-called undeveloped reserves, and a part of its so-called developed reserves) was not actually used and useful in the present public service, and would not become useful at any reasonably near time in the future so that in reason and justice it could be considered in the nature of presently necessary working capital. *Columbus Gas & Fuel Co. vs. Pub. Ut. Com.*, 292 U. S. 398, 406-407, 78 L. Ed. 1327.

The Company's method of including all production system properties in the rate base and of placing grossly exaggerated valuations thereon was objectionable for every reason which impelled this Court to condemn such method in *United Fuel Gas Co. vs.*

Railroad Com. of Ky., 278 U. S. 300, 310-322, 73 L. Ed. 390, and for additional reasons which we shall now endeavor briefly to set out.

Company witnesses have evaluated what they called developed or marketable reserves in proven and semi-proven areas, by estimating the volume of gas in place beneath the surface. This valuation was arrived at by assuming that the entire volume would be exhausted over a period of 20 years in the future, and that the rate of withdrawals from Company reserves and the prevailing field prices of gas would increase progressively throughout the 20 year period. The assumed rate of withdrawals in the future was shown to be as much as four to five times the rate of withdrawals in the past, up to the time of the District Court trial, R. I, 107, 531, 577; III, 2124A, 2165.

Based upon Dunn's estimate of the future rate of withdrawal, Company witness Hulcy evaluated the developed reserves in the proven and semi-proven areas, R. I, 531, 576-577. Hulcy took the estimated volume of gas and determined what it probably would be worth, if presently marketed, in all fields except the Texas Panhandle and Petrolia fields.

In the Petrolia field there was no gas being sold so as to establish a prevailing field price, and Hulcy in lieu thereof assumed a price of 10c per MCF; which, he testified, had been established by the Federal Government for income tax depletion allowance in the war time period of 1917, R. I, 589. In the Wheeler County, Texas, field, where the overwhelmingly major portion of the Company's developed reserves is located

he assumed future rates of withdrawals over an estimated future 20 year period of production at a rate of withdrawal 4 or 5 times as great as the rate of withdrawals had been up to the time of the trial, and also assumed progressively increasing field prices over that period R. I, 107, 531, 577, 559-560; III, 2124A, 2165. From this total estimated valuation of Wheeler County reserves he deducted the estimated cost of present gas well construction and equipment, and assumed that 135 additional wells would have to be drilled in the future to produce the gas over the 20 year period and deducted from the estimated total the estimated cost of present and assumed future cost of gas well construction and equipment, less totally inadequate assumed salvage values; and to the remaining estimated value he applied an assumed present worth factor of .46319, (8 per cent compound interest basis), R. I, 561-566.

It will be perceived that all of these basic assumptions were in the highest degree speculative, conjectural, uncertain, and inaccurate and not supported by any substantial basic factual data. It will be seen also that the greater the rate of assumed future withdrawals and the greater the assumed future field prices, the shorter would be his assumed period of production, and the greater would be his assumed present worth of the reserves, R. I, 578-581.

The whole method involves in essence the capitalization of assumed speculative future earnings (R. III, 1659-1660) and is the identical scheme of evaluation which was condemned by this Court in *United Fuel Gas Company vs. Railroad Com. of Ky., supra.* The

Commission's witness Phillips, an accountant of broad experience, testified in respect to the question of the Hulcy method being capitalization of future earnings:

"Q. I will ask you, Mr. Phillips, if the method used in finding the present fair value of net gas reserves as calculated by Mr. Hulcy is not what accountants ordinarily understand and mean as being a capitalization of future earnings?

A. Well that is my accounting understanding of it and I believe it is the general understanding of accountants generally," R. III, 1659-1660.

It is pertinent to say that the valuation arrived at by Company witnesses of the production system properties was grossly excessive over the actual historical book cost of these properties.

As to the so-called undeveloped reserves, situated in unproven territory, the Company witnesses made no estimate of the volumes of gas in place, as they had no way of knowing that any gas was actually located under the leases at all, (R. II, 835) but these properties were evaluated by Company witness Steinberger, as per Steinberger's exhibit showing such leases, upon the basis of original acquisition costs as per books, plus all other costs incurred in connection therewith as per the books, such as delay rentals, etc., R. I, 570-572.

It is obvious that none of this property, estimated by Steinberger at $893,291.28 (R. V, 3034A), and given blanket endorsement by Biddison, (R. I, 654-655) is presently used or useful; it is certain that it will not become used or useful at any time in the reasonably near future, in view of the undisputed fact that the so-called developed reserves are sufficient at

past rates of withdrawal to last from 40 to 60 years; and it is doubtful whether they ever will become used or useful, especially in view of the admitted fact that it is not known whether they contain gas or not, R. II, 835.

The Company charges all costs of these leases into operating expense as cancelled and surrendered leases if the leases prove worthless; but on the other hand if gas is discovered and developed thereon the Company gets the benefit of the discovery by including the estimated value in the rate base at highly excessive figures. The Company gets all the profits of enhancement, and the consumers bear all the losses. This enhanced value of the proven leases is much more than sufficient to include the cost of the leases ultimately condemned. Yet the Company takes all the benefit of the enhancement due to actual development, by including the proven leases in the rate base at their enhanced value, but loads upon the rate payer, in addition thereto, the total cost of all the condemned leases by charging the cost thereof into operating expenses, R. III, 2126A. And in the meantime, until the undeveloped reserves ultimately are either made valuable and included in the rate base as developed reserves, or condemned and charged off into operating expense, they are included in the rate base at book cost.

In this connection we beg to refer also to our discussion of cancelled and surrendered leases as an operating expense, supra, pp. 122-124.

The Company includes *undeveloped* leaseholds in all of its appraisals at book cost, including $200,-

199.39 delay rentals. It was not shown that any of these leaseholds would be developed in the reasonably near future. R. V, 3034A, I, 568-575. The Commission also included in its rate base the undeveloped leaseholds, including delay rentals, at cost. R. I, 70-72, 570. It is held in *Columbus G. & F. Co. vs. Pub. Ut. Com.*, 292 U. S. 398, 406, 78 L. Ed. 1327, that it is not proper to capitalize delay rentals on such leases. The Company and the Commission included in operating expenses the cost of charged-off cancelled and surrendered leaseholds and dry hole expense. R. I, 28-29, III, 2208-2294.

Developed leaseholds were included in the rate base by the Commission at the actual cost of the leaseholds under one set of computations and, under another set of computations, the developed leaseholds were excluded from the rate base and the Company-produced gas was allowed for at the prevailing field well head price. Under either method of computation, the return averaged in excess of 8% for the years 1927-1932, inclusive, considered by the Commission. R. I, 20. In evaluating developed leaseholds and production property the Company purported to proceed upon the following assumption: "We are assuming that our own gas reserves are worth exactly the same, or that the gas produced by the Company in any field is really worth exactly the same as that purchased from any other producer. It is worth that much and no more, and we have gone about it on that assumption." R. I, 72, 594. The Company then proceeded, however, to capitalize the value of its production properties based upon future estimated withdrawals and assumed future increased field prices. R. III, 1659,

1660, V, 3031-3032. However, in respect of its principal reserves (Panhandle District of Texas), instead of using the prevailing field well head price of 2c per MCF, which is now being paid and which has always been paid in the field (R. I, 581-582), the Company more than doubled this price and assumed that the gas was worth 4.7c per MCF. R. V, 3032. If, instead of assuming a value of 4.7c per MCF, the Company had proceeded on the basis of 2c per MCF, the prevailing field price and the price being paid other owners by the Company in the Panhandle Field, the gross value of the Panhandle production properties as shown on R. V, 3032, would have been reduced from $9,933,-969.00 to $4,227,621.00, (R. I, 585) and the estimated net recovery value of the gas reserves as shown on R. V, 3031, would have been reduced from $16,055,292.00 to $10,348,944.00. The Company further assumed that it would withdraw this gas at the rate of 20,000,000 MCF per annum as compared with its actual withdrawal rate of from 5,000,000 to 6,000,000 MCF per annum. R. I. 107, 564, 576-577. If, instead of using a 20,000,000 MCF withdrawal rate in the future, the Company had used a withdrawal rate of approximately 12,000,000 MCF per annum, or more than double the actual withdrawal rate, the present worth discount factor would have been .31524 instead of the assumed present worth discount factor of .46319. R. I, 579. By applying the .31524 present worth factor to the net recovery value of $10,348,-944.00 based on the actual prevailing field price, we arrive at $3,262,401.00 as the present fair value of gas reserves including gas well equipment and construction. This compares with the present fair value

of $7,436,650.00 found by the Company (R. V. 3031) and which figure was used in all of its appraisals before the District Court. The Company used a present worth discount factor of .368 for the Texas Panhandle (Wheeler County) Field in its testimony before the Commission. R. I, 581. It is by means of these involved speculative and erroneously unjust calculations that the Company takes gas worth less than 5c per MCF (4.82c per MCF) and finally charges it into its rate base, depreciation and depletion charges and into operating expenses in such a way that it would cost 23.3c per MCF at the well head. See pp. 144-145, supra.

Proceeding on the basis that the Company-produced gas was worth what the gas could be purchased from other owners for, (the Company purchases approximately 72% of its gas, R. I, 74; Freese testified before the District Court approximately 80% is purchased and 20% produced, R. III, 1894), it would have been a great deal simpler and more just to charge directly into operating expenses the prevailing field well head price for the Company-produced gas. This was what the Commission did under one of its sets of computations (but did not adopt as a basis of fixing the rate), and also what the Commission witness did before the District Court. If the Company's capitalization of the value of its production properties and its estimated withdrawal rate had been in accordance with the actual facts it would have arrived back, at the end of its complicated and intricate calculations, at the prevailing field well head price of approximately 5c rather than 23.3c per MCF. The Company could

purchase all the gas it requires in the Panhandle field at 2c per MCF.

The Company should either (1) accept an actual cost basis for the appraisal of both undeveloped and developed leaseholds and charge the actual cost of bringing the gas to the well head and of cancelled and surrendered leases and dry holes, to operating expenses; or, (2), they should charge for the gas at the well head at the current prevailing field well head price. The Commission made computations on both of these bases. If the Company had correctly made its computations, its results would have been the same as using the prevailing well head price, with the exception of the fact that they would still charge cancelled and surrendered leases and dry hole expenses into operating costs. This latter exception is improper, inasmuch as the prevailing field well head price paid the other owners includes all cancelled and surrendered leasehold expenses, all dry hole expenses, depletion and depreciation, R. I, 599, 600, 28, 29, 67, 68.

We are perfectly willing to accept the Company's original basis of treating developed production properties, where it finds that its produced gas is worth the same as what it could buy gas for in the same field from other owners. However, this basis should be strictly adhered to in all of the resulting computations and its approval should not be inflated beyond this basis by in excess of $4,000,000, as has been done in this case, nor should operating expenses be made to bear the cost of developing these gas reserves, the value of which the Company now wishes to capitalize. Further the present users should pay only for

the Company-produced gas they use (5,000,000 to 6,000,000 MCF per annum) and not for a greatly increased amount (20,000,000 MCF per annum) as estimated by the Company witnesses, R. I, 74.

The Company claims on page 13 of its brief that the Commission eliminated from its rate base capital additions to the property made in the year 1932 in the amount $2,257,682.07. By referring to the pleadings in the state trial court (R. I, 142), the Company also claims that the Petrolia field account in the amount of $687,781.13 was "arbitrarily and capriciously eliminated". The $2,257,682.07 figure was made up of the cost of the Southern Oil and Production properties of $966,600.11 (including $200,000.00 "value of contract", R. III, 1603) and of the undepreciated original book cost of the Meridian Gas Company at $1,338,406.21, R. I, 343, 460. The Commission did include the prorata cost of the Southern Oil and Production properties in their rate base for the year 1932, the property having been purchased on October 1, 1932, and in the Tables, infra, which we are submitting, these properties are included for the year 1933 at their full cost.

As to the inclusion of the Meridian Gas Company properties, the Commission states, *"Neither the Company witnesses nor the witness Freese submitted an appraisal of these production properties.* We have allowed not only the actual production expenses but also fifteen cents per M. cu. ft. for the gas produced during 1932 as a return on this property. In other words, if instead of purchasing the property the Lone Star Gas Company had continued

to pay the very ample price of 15 cents per M. cu. ft. to the affiliated Meridian Gas Company, the 1932 operating expenses could be eliminated from the 1932 computations." R. I, 110. The Commission allowed for the gas produced from the Meridian properties, in addition to allowing all operating expenses, the sum of $70,227.30 for the year 1932. R. I, 108. The Meridian holdings comprise the production properties and gathering system in the Chickasha field and a short section of transmission line. Appellant acquired this property for $1,300,000.00 plus, from the Lone Star Gas Corporation on January 1st, 1932. R. I, 110, 343, 460, 461.

As to the estimated value of these properties, as per the Company witness, refer to R. V, 3032. It is there to be noted that the gross value of the Chickasha, Oklahoma reserves is $173,079.00, including all gas reserves, production gas well equipment, production property of every kind and including all recovery operating costs. Referring to R. V, 3031-3032, and without deducting the recovery operating costs, it is seen that by applying the present worth factor of .46319 (as used by Hulcy) to the gross value of $173,079.00 we have a present fair value of gas reserves, including gas well equipment and construction, of $80,168.00. This is the Company's own appraisal of the production properties and clearly shows that the Lone Star Gas Corporation sold the properties to its subsidiary, the Lone Star Gas Company, for $1,300,000.00 plus for the simple purpose of putting these properties in the Appellant's rate base, and it is largely with reference to these properties that the Com-

pany complains, on page 13 of its brief, that they were eliminated from the Commission's rate base. This is true in spite of the fact that the Commission allowed all operating expense plus $70,227.30 for the gas delivered by Meridian Gas Co., which latter sum is a return of 5% plus on the fictitious value claimed for these properties which the Lone Star Gas Company places in its various rate bases.

With reference to the Petrolia field account in the amount of $687,781.13 claimed by the Company as a part of its rate bases, the Commission found, and the Company in no way refuted the finding in the District Court, that the cost of getting the gas to the wellhead in the Petrolia field was in excess of the full value of the gas at the wellhead and that instead of this field having any value as used and useful public service property that it was a liability, R. I, 46-47; III, 1739. Based upon the Company's method of evaluating gas reserves and allowing for the gas at 10c per MCF, the Company found a negative value for this field. R. I, 590. We cannot escape the conclusion that the Petrolia field is being operated at a loss simply for the purpose of including its reproduction cost in the rate base.

It is to be noted in Tables II and III, infra, which we are submitting, that in the use of undepreciated book costs as rate bases, no deduction of the Petrolia field account and of the cost of the Meridian Gas Properties has been made. Furthermore, it is to be noted in Table II, infra, where the rate base as found by the Commission is used, that the Meridian Gas properties are included at book cost.

"Omissions and Contingencies" and "Duplications": These constitute another inexhaustible source of padding tapped by the Company's witnesses. On practically every item entering into direct structural cost, Biddison added substantial percentages for omissions and contingencies, even super-adding them into his developed unit costs purportedly based upon actual costs as incurred and studied. His theory was that there would be omissions from the inventory of property, which he testified was as complete and exact as it could practicably be made, (R. I, 614); and that contingencies would occur in a reproduction new which had not been encountered in the original construction, and which would increase the cost. When cross-examined as to whether the inventory might not as reasonably be expected to include duplications rather than omissions, and as to whether the unit costs as developed from studies of actual construction would not necessarily embrace all omissions and contingencies, Biddison replied, "So far as I know, nothing was omitted from the original study. It was not designed to have anything omitted from the original study. But, in the analysis of cost data you determine only the cost of the things from which the data was derived. When you go to apply that cost data to the construction of something else, at different locations, under different conditions, it is good judgment to allow for differences in those conditions that may cause differences in costs and any estimator who does not do that is courting disaster, either for himself as an estimator, or for the people who use his estimates as the basis for bids in trying to finance a proposition," R. I, 689. He admitted that he had made no effort to relate the

unit costs in his appraisal to the actual cost as historically incurred and as shown on the Company's books, R. I, 669.

At R. I, 662, Biddison testified:

"Q. Then you didn't look at the actual records of the Company to make that statement?
A. Certainly not.

Q. You were not even interested in it, were you?
A. No."

Further, at R. I, 750, Biddison on cross-examination testified:

"Q. Well, have you or anybody else, Mr. Biddison, for the purposes of this appraisal, tried to relate the prices or the costs you have actually used in your appraisal, to the costs of the Company on the books?
A. No."

Upon this basis, he added 2½% to all detailed costs of transmission line equipment on all lines throughout the system, R. I, 647; II, 766, 806. This item amounts in Company Exhibit 28 to $681,-416.72 on transmission system properties only. R. III, 1957. His unit costs on this item purported to have been developed from actual time studies on the system of the Lone Star Gas Company. On gas well construction, he added a contingency item of 24.75c per foot over costs actually incurred in this class of property, R. I, 617, 621, 689. This item was added to the Company's actual experience of $1.3017 per foot, making $1.5492 per foot used in his appraisal. These

additions included contingencies ranging from 15% to 25% of actual costs on individual items going into well equipment and construction. R. I, 687-690. To the Company's actually incurred historical cost of acquiring rights of way for transmission and gathering lines, he added 20% for contingencies. R. I, 637.

Company witness Dyer, sole witness as to reproduction cost of general office building, included a profit of 8%; included 5% for contingencies in the amount of approximately $13,000.00 in case the owner should change his mind as to plans, notwithstanding construction contracts uniformly provide that the owner shall pay additionally for such changes; R. I, 677, 678-680. He testified that he did not include any such contingencies in bidding on an actual post office job at Chattanooga, Tenn. R. I, 684. Dyer also included 3% for contractor's overheads, R. I, 678.

On installation of field measuring stations, Biddison used hypothetical gangs and 2½ % for omissions and contingencies. R. I, 710-711. For installation of drips, 5% contingencies, R. I, 744. On installation of field line equipment, 5% contingencies, R. II, 1173.

Biddison was asked several times to ascertain or estimate the total amount of his omissions and contingencies but testified he was unable to do so and that he had made no effort to do so but thought it was less than $1,000,000.00, R. I, 734-736; II, 806-807.

On cross-examination Biddison testified (R. II, 806-807):

"Q. You have been asked the question heretofore, Mr. Biddison, as to what the approximate amount of the total omissions and contingencies in your whole appraisal is. Have you figured that out yet?

A. No, I have not given it any consideration since the question at all."

On unloading, hauling and stringing of pipe, Biddison added contingencies of 10c per ton for handling through stock piles, not shown to have been historically incurred, and 5.7 cents per ton for gangs moving from job to job although these costs had been already included in actual cost estimates; also 10% for contingencies, and an additional 5% on the overall figure for contingencies and omissions, R. I, 734-736; III, 1767.

Commission witness Freese testified that the Company has included omissions and contingencies in an approximate amount of $1,000,000; that practically all of the Company's studies were based upon actual construction costs which included omissions and contingencies actually encountered; that he has checked some two million feet of pipe purchased against length shown in appraisal and that they were almost identical, so there could be no omissions and contingencies on transmission line pipe, on which Biddison allowed 2½ %, or $797,360.98; R. III, 1746-1747, 1780.

Commission witness Freese eliminated the 20% contingencies added on transmission line rights of way, by Biddison, because they had not actually been incurred by the Company, R. III, 1741-1742, 2146-2147.

In addition, the record reveals instances too numerous to specify here, where the Company's witnesses obviously included duplications between various capital items, between capital items and operating expense items, and between operating expense items and depreciation accrual items.

"Preliminary Development and Organization Costs": We have previously pointed out that the Company witness Connor added approximately $24,000,000.00 to the Company's estimated direct structural costs, to cover preliminary, organization and development expense, undistributed general overheads, working capital and going concern value.

A reference to Appellee's printing praecipe, R. V, 3529, will show that the Company did not request the printing of that portion (volumes 7 and 8) of Company's Exhibit 28, setting forth the basis on which Connor founded his estimates of these items. We do not blame the Company for attempting to keep the contents of that astounding treatise from coming to the attention of this Court. The utter prolixity, unintelligibility, and lack of perspicuity of the witness' attempt to explain his methods of approach can only be appreciated by an actual reading of the record, R. IV, 2602-2921.

The appraisal prepared by Biddison, Steinberger and Connor pre-supposes an outlay of $4,474,272.00 covering costs for "Preliminary Development and Organization Costs" to be hypothetically incurred in a reconstruction of the Company's properties; however, this does not include any item of such esti-

mated costs in connection with leaseholds or producing wells, transferred by the originating group to the corporation that is to be formed under Connor's proposed plan of organization, R. IV, 2606.

The present financial structure, and something of the past history of same, is briefly summarized by Commission's accountant Phillips, R. III, 1876-1879. The Company was originally incorporated in 1909 with $2,500.000, $100 par-value shares, R. III, 2176. This was partially paid in leases in Petrolia Field, R. I, 422-426. The present capital set-up consists only of 540,000 non-par value common voting shares, with no outstanding preferred stocks, bonds or other senior securities. The capital has been provided, and the property built up, only by issuance of capital stock for cash or property, by the borrowing of money, by the use of accumulated and undistributed earnings and by the use of the depreciation reserve. Only $12,500,000.00 has been paid in by stockholders, in cash or property. Something in excess of $28,000,000.00 is set up on the books as representing the non-par value shares. That includes an allocation of surplus earnings and an allocation of re-valuation surplus. Surplus on the books is now $8,000,000.00 or $9,000,000.00, R. III, 1876-1878. See the summary of the Company's financial history as found by the Commission from Hulcy's testimony, R. I, 64-66.

As against this very simple capital structure, Connor in his assumed reproduction cost sets up a complicated and ridiculously excessive capital structure consisting of an assumed issue of first mortgage bonds

of $38,000,000.00, preferred stock of $19,000,000.00 and common stock of $17,000,000.00, R. IV, 2637. Of the $4,474,272.00 estimated by Connor (R. IV, 2606), $4,050,000.00 is made up of cost of marketing securities and "remuneration for the originating group" which latter item alone is $2,000,000.00, which he assumes the promoters would take out in common stock. These costs have been condemned by this Court in *Los Angeles G. & E. Corp. vs. R. R. Comm. of Calif.*, 289 U. S. 287, 310, 77 L. Ed. 1180, 1195, as being "too conjectural to be allowed."

Connor, in preparing his estimate of this item of cost definitely and wholly disregarded the Company's history, as to whether or not any such costs have been historically incurred, or as to the manner and means under which the Company came into possession of its properties, even going so far as stating, "They might have charged the Company's office building to operating expenses, for all that I know", R. II, 1036.

Of the several items entering into this estimate, preliminary engineering and geological investigation total approximately $200,000.00. Connor says that the investigation of these two items would be absolutely necessary in connection with the reconstruction of the Company's properties at this time, as the organizers would proceed on the theory that none of the engineering or geological problems that would confront the Company had been solved; that the geological body that would be organized under this preliminary organization would have no knowledge or information of any character whatsoever as to the presently existing unlimited reserves of natural gas

available throughout the Texas Panhandle area. According to Connor it would be extremely doubtful whether they would even know that a gas field actually exists in Texas; R. II, 1029-1030.

Although Connor states that he is aware of the fact that discount on the proposed issue of securities cannot be (and he claims that it has not been) included by him as an element of cost entering into the reproduction cost new of the Company's properties, he nevertheless takes into consideration the fact that in the sale of the proposed issues of securities such securities would necessarily have to be sold at a discount in order to secure their ready sale, and he actually included a discount of 10% in his "interest during construction", R. II, 979-980.

Biddison and Connor both, in estimating their costs, gave no consideration whatsoever to the substantial savings to the Company on all items of cost which would be brought about by its affiliation with Lone Star Gas Corporation; the record showing that the Corporation has lent money to the Company on open, unsecured notes, as and when needed, at 6% simple interest; these advances amounted to about $19,000,000.00 at their peak, a few years before this rate case. They had been reduced to $17,600,000.00, at the time of the trial, R. I. 412.

In connection with the estimated cost of "Fiscal Agents Title Certification" in the sum of $25,000.00, Connor admitted that the Lone Star Gas Corporation had always acted as the fiscal agent for the Company

and that the Company itself had never incurred or actually paid out any such expenses, R. II, 1036-1037.

On cross-examination, Connor testified:

"Q. Why didn't you assume, Mr. Connor, that the Company would be organized just as it is organized, as a subsidiary of Lone Star Gas Corporation?

A, Because I think it is proper to make the estimate upon the basis of the reproduction of this particular property without reference to its connection or affiliation with any other property or properties. I don't know that that relation would affect the cost of its reproduction in any particular." R. II, 1037.

Administrative and Legal Expense: The total amount of estimated costs for this item is $2,347,595.00, and covers the amounts estimated to be incurred after the organizers of the proposed company had assembled their preliminary data and started actual construction of the Company's property. This cost estimate is apportioned between executive, legal, accounting, treasury, land, geological, and purchasing divisions, each of which is set out in detail at R. IV, 2659-2779. It presupposes an elaborate set-up of administrative officials and legal and accounting personnel, that does not bear even a remote resemblance to the Company's history or operations and is in fact one of the most speculative and excessive of all of Connor's undistributed general cost estimates.

These elaborate estimates were made by Connor even though the books of the Company show that this

item is being capitalized upon the basis of 2% of the actual cost, R. II, 1750.

General Engineering Costs and Reproduction Costs of Final Engineering Records: Connor estimates General Engineering Costs at $1,127,661.00. R. IV, 2780. He contemplates a four-year period of engineering work. It does not include the engineering costs that were incurred prior to incorporation of the Company, which costs are specifically set up under "Preliminary Development and Organization Cost," nor special fees paid for the designs of special structures, nor engineering costs directly charged by Biddison to specific property accounts in the estimate of the direct structural cost of the physical property, R. II, 955; IV, 2781. Nor, does it include the item of reproduction cost of final engineering records, which latter item is included in and made a part of direct structural cost of physical property, R. II, 954.

The estimated cost of final engineering records is set up at the sum of $765,690.35, R. IV, 2780. The combined general engineering work and the cost of final engineering records would contemplate a hypothetical four-year period for their completion. There would be 3 years of preliminary work and 3 years of final engineering work. For 2 years the preliminary engineering and the final engineering would be carried on concurrently, R. IV, 2781. Charging draftsmen's time at something in excess of $1.00 per hour, it was shown that according to Connor's estimates the final engineering drawings would in many instances exceed in cost, by several times, the cost of constructing

the object of which it was a drawing. For instance, chicken houses, cattle guards, water faucets, etc., R. II, 1085-1088.

The item also includes the assumed expense of "house counts" (made in the *cities* being served natural gas), although no such expense was ever incurred by the Company in any city in Texas, (R. II, 1092-1093) and although this expense, if incurred, should be included in distribution operations and borne by the distributing companies, and although he (Connor) would duplicate this expense in evaluating the distribution properties, R. II, 1116-1117.

General Supervision of Construction Costs: Connor estimates the cost of this item at $414,493.00, R. IV, 2654. It embraces the cost of salaries and expense of the general superintendent and his office organization; the expenses of the superintendent of plant and equipment and his organization and the expenses of the supervisor of safety and medical examination, R. II, 960. These charges have been segregated from the other supervisory charges for which separate estimates have been made in the appraisal. Connor considered them to be general in their nature and, therefore, in his opinion they did not lend themselves to allocation to specific properties, R. II, 960.

General Supervision Allocated to Specific Property Accounts: In addition to the said cost of general supervision, Connor sets up *another* estimate of supervision cost which he says is not allocated to specific property accounts. This item totals $425,634.00, R. IV, 2880. These two items of so-called supervision

charges are set up by Connor in addition to the estimated cost of supervision of job foremen which is included in the unit cost developed by Biddison and reflected in the direct structural costs of physical properties (R. II, 961), thus making a total of 3 different supervision estimates that enter into Connor's pyramided supervision cost structure. This $425,634.00 overhead item is included by the Company as a "direct cost" and made to appear as an inherent part of the physical property, R. IV, 2366 2368.

Taxes During Construction: The Commission findings in the amount of $9,681.29, appear at R. I, 48. The taxes are estimated by Connor at a total of $173,881, R. IV, 2367. He testifies they are intended to cover all expenditures in connection with the state, county, city and other taxes that would be levied and paid on the property of the Company during construction and before the facilities would be used for operation, R. IV, 2941-2942. Although Connor further stated that he did not know the amount of the taxes paid by the Company, historically, in connection with the construction of its property, and was unable to say whether any taxes were paid during the construction of the Dallas Gas Company Building, or the Lone Star Gas Company Building, (R. II, 1099), he, nevertheless, takes the position that the total amount of this item of cost would necessarily be incurred by the Company. He definitely admits that he gave no consideration or attention to the fact, as to whether the Company actually or historically paid any taxes whatsoever during the original construction of the property, R. II, 1100.

Freese, on the other hand, testified that the history of the Company disclosed that very little, if any, taxes were *actually* paid by the Company during the period of the construction of its properties, (R. III, 1753), he stated further, that the Company's own records disclose that during the years 1927 to 1929, at which time $17,000,000 of its construction work was carried on, only $1,616.73 was actually paid by the Company for taxes accruing during the said construction period, R. III, 1754.

The Company's actual experience, in recent years, clearly shows that the amount of taxes paid by it, proportionately, on the amount and value of the property then under construction, does not justify the inclusion of any hypothetical item of cost in the sum as here set up by Connor in his aforenamed Exhibit.

Interest During Construction: This item of cost is estimated by Connor at $4,975,933.00, R. IV, 2654, It represents the estimated cost of interest charges incurred from the date of the incorporation of the Company, until the property will pass from construction into operation, R. II, 975. In connection with this item Connor again assumes that 50% of the money required in the reconstruction of the Company's properties would be raised by the issuance of first mortgage bonds, 25% by the issuance of preferred stock, and the remainder by the issuance of common stock; and this, again, in the face of the known history of the Company that no such securities were ever issued by it, either in connection with the original construction of the first unit of its property, or at the time of the construction of any later units. Connor further assumes that the Company would be required to pay

interest at the rate of 8% per annum, although it is paying only 6% per annum for all sums of money borrowed by it, (R. II, 1107), the difference being made up of discount on senior securities.

Working Capital: Connor estimated this item at $1,701,600.00, R. V, 3005. This includes materials and supplies on hand in the amount of $555,000.00 at inventory prices and book cost, about which there is no complaint; allowance is also made of $255,000 to cover 45 days operating requirements, (R. V, 3006) which is not questioned. Included, however, is an item of $300,000.00 for cash balances in bank, R. V, 3006. We question the propriety of this last named item, as it is not shown that the banks require the maintenance of any cash balances in order to obtain banking services without charge. The current practice is that banks require no more than 10% of current borrowings to be maintained on deposit; and as the record shows that the Company's current, outstanding, short term loan with its Dallas banks, amounts to only $25,000 (R. III, 1964), and that the largest sum ever borrowed from banks, by the Company at any one time, was around $500,000 for a very short period of time, (R. III, 1969), a bank balance of approximately $50,000 would be the maximum amount that would ever be required to be set up for this element of cost. This Court can take judicial notice of the fact that the Interstate Commerce Commission allows only 45 days operating expense, without the addition of bank balances or other items.

Going Concern Value: Connor estimated this item at $7,792,888.00, R. IV, 2957. He based it primarily upon development costs in the initial stages

of the business—that is, fixed charges (depreciation, interest and taxes) upon idle plant, plus 10% net return (R. II, 1005) upon such idle plant as was estimated not to be carrying its full capacity load of business during the period of initial business development, pending attainment of normal customer attachment and customer consumption by the distributing companies served by Appellant, (R. II, 1004-1006). It was not shown that any such business development costs were incurred in the initial stages by the Company; but on the contrary, the financial history of the Company, as found in the opinion of the Commission, (R. I, 65), shows that the Company has been phenomenally successful in obtaining profitable business from the very beginning, R. III, 1755, 1803-1804, 2108. The Commission said: "To summarize our conclusions . . . we find the allowance of going value determined by . . . Connor, to be without any sanction in . . . . . reason . . .", R. I, 66.

The Commission further said: "We find * * * that the adoption of the reproduction cost new value as determined by us * * * containing, as it does, a complete allowance for all overhead expense, together with our allowance for operating expenses, fully and justly compensate the Company for all development costs which have been incurred or which would be incurred on a reasonable reproduction of the Company's properties and that such an allowance thus determined is ample to cover any and all items entering into and forming a part of going value." (R. I, 66, 52-66).

Connor also included an estimated cost of attaching customers, of obtaining new business and of training

the personnel in operating routine, etc., all of which were shown to have been charged to operating expenses and recouped by the Company, from the beginning of its history, R. III, 1645, 1803.

He attempts to differentiate his method of determining the existence and amount of going concern value, from the "past deficit method" (R. II, 1004-1005) and says that he has not estimated, or included, "any losses" of past operations by reason of inadequacy of rates, or otherwise. This is an obvious attempt to distinguish his theory from the methods condemned by this Court in *Galveston vs. Galveston Electric Co.*, 258 U. S. 388, 395, 66 L. Ed. 678, 683, where it is said that "past losses, obviously, do not tend to prove present values", and many other cases by this Court, following and applying that doctrine, down to the present time.

A careful reading of Connor's entire theory of Going Concern Value will reveal that it is identical with those methods rejected in the *Galveston* case; and, lately, in *St. Joseph Stockyards Co. vs. United States*, 298 U. S. 39, 62-64, 80 L. Ed. 1033, 1047-1048.

In his elaborate theorization, he utterly disregards the history of the Company, saying expressly that he does not know what the history is, has made no effort to find it out, and would have paid no attention to it if he had known it. He also says it would have made no difference to him, if the Company had been charging to operating expense and had fully recouped in the past all of the expenses which he used as a basis for measuring the claimed Going Concern Value, R.

II, 1134-1135. In so doing he goes squarely in the face of this Court's holding in *Houston vs. Southwestern Bell Tel. Co.*, 259 U. S. 318, 325, 66 L. Ed. 961, 965, where it is said, "Whether Going Concern Value should be considered and allowed at all in determining the base for rate-making, and, if allowed, what the amount of it should be, depends upon the financial history of the Company."

Furthermore, in determining and estimating this claimed element of value, Connor forgot the Company's position, asserted in connection with its interstate commerce contentions, namely, that it was a totally different entity from, and not in any way related to, its affiliated distributing companies.

Both Connor and Biddison, in assuming the destruction of the Company and all its properties, for purposes of reproduction, destroyed not only the Company and its property but also the personnel; also the distributing companies, and all of their property; and even the 230,000 domestic consumers who are customers, not of Appellant, but of the distributing companies, which customers he treats as being customers of the pipe line company. The only exception is the city of Fort Worth, where the Appellant carries on distribution operations directly serving approximately 33,000 retail customers, R. III, 1896.

Not content with going that far, he goes even to the extent of assuming that these 230,000 customers and all of their gas appliances and equipment have been destroyed and would have to be replaced, also. But

his audacity is not even yet exhausted. He admits that, having taken into consideration the supposed value of having these 230,000 retail customers attached to the distributing companies, who are not customers of the pipe line company at all, that he would, in any burner tip case involving any one of the distribution companies, duplicate this going concern element by including customer attachment and customer use value in the burner tip cases, also, R. II, 1115-1120. Under his theory, the more customers that were attached to the distributing companies, and the more gas per customer they used, the more valuable would be the properties, not only of the distributing companies, but also of the pipe line company; and, therefore, the higher the rates that would have to be paid by the customers, as the number of customers and the degree of customer use saturation was increased, R. III, 1118. This Court has never sanctioned the use of any such vicious circle as a basis of an element of value to be included in a rate base.

Typical of the Company's methods before the Commission and all courts, is the claim on page 145 of its brief, that "Appellees include nothing in their appraisal for going concern value". Counsel quote a single question and answer, from the testimony of the Commission's witness Freese (R. III, 1793-1794, 2108), which, standing alone, would support the statement. By referring to the record pages cited, however, this Court will see that the Company has affirmatively and deliberately misrepresented to the Court what the testimony was. At R. III, 1793-1794, appears the following testimony:

"Q. You made no separate allowance in connection with your Exhibit 6 for Going Value, Going Concern Value, or Cost of Reproducing the Business did you?

A. No.

Q. Was it your testimony that you had, nevertheless, allowed something for Going Value?

A. No; as I recall my specific statement, it was that we had priced everything as usable, as something that was in use, or could be used, and not something that had no business or no use, or was junk value, or something to that effect."

Then follow the question and answer, quoted by the Company on page 145 of its brief; and at R. III, 1755 appears the following testimony:

"Q. Now then, I notice in your non-physical properties, and in fact, nowhere in your summary is there a separate allowance for going concern value, or going value. Does that mean, Mr. Freese, that you have not evaluated this portion of the Company's property as a going concern?

A. No; that does not mean that we have not taken this at its reproduction cost new as a going concern, rather than its junk value as a going concern.

Q. Why have you felt justified in not making some sort of additional and separate allowance for going value?

A. In the first place, the history of the Company indicates that no losses on idle plant were actually incurred; or if any such losses were incurred during the earlier years of the Company, that they have been easily made up in the meantime. In the second place, during the operating periods considered in the auditors exhibits, most of the items which are ordinarily considered as

contributing to the building up of going value have been charged to operating expenses."

And at R. III, 2107-2108, occurs the following:

Q. Well, if the title is to be taken as it reads where have you included any allowance for going value, going concern value or cost of reproducing the business?

A. Mr. Griffith, I have not *separately* labeled a certain amount of dollars as going value. Every item included in there is property, as part of a going concern. Furthermore, in addition to that, in the operating expenses which we have allowed, we have allowed for the attachment of new business, the securing of new business, advertising expenses, and every expense that would be incurred in the nature of attracting new business and which is one of the things which ordinarily, and which does go to make up what is known as going value.

Q. Now, we may get to the profit and loss statement, later, Mr. Freese, but please confine yourself to this reproduction cost evaluation at this time. Can you point out to me a single dollar in here, or a series of dollars which represents going value, going concern value or the cost of reproduction of the business as distinguished from the cost of reproduction of the property?

A. Not *separately* labeled as such, no.

Q. If the property of the Company were to be reproduced as of June 15, 1934, and there was no business attached whatsoever, wouldn't your reproduction cost be the same as set forth in plaintiff's Exhibit No. 6?

A. Yes, and that would be true whether it was 100 per cent saturation or whether there was no saturation at all, *in view of the history* of the

> Company, the way it was actually produced and the way it could be produced from the beginning again. *There was no loss of return on idle plant during the history of the Lone Star Gas Company.*" *Italics ours.*

Freese's method of valuing all of the component parts of the property, as parts of an active, going concern with all business fully attached, personnel trained, and all undistributed general overheads and other intangible values fully allowed for, instead of making a *separate* lump sum estimate of going concern value, as such, has been repeatedly approved by this Court, more notably in *Los Angeles G. & E. Corporation vs. R. R. Com. of Cal.* 289 U. S. 287, 302-303, 313-319, 77 L. Ed. 1180, 1191, 1196-1200, and cases there cited and reviewed; and also in *St. Joseph Stockyards Company vs. United States*, 298 U. S. 38, 62-64, 80 L. Ed. 1033, 1047-1048. And see especially *Columbus G. & F. Co. vs. Pub. Ut. Com.*, 292 U. S. 398, 410-413, 78 L. Ed. 1327, 1334. These cases condemn the Company's methods as to this item.

Per Cent Condition: The Commission used the sinking fund method of depreciation accrual accounting and, therefore, used an undepreciated rate base. The same method was used by Freese in his testimony both before the Commission and the District Court. On the other hand, the Company's witnesses purported to use, in their testimony both before the Commission and District Court, the straight line method of computing depreciation, and a depreciated rate base. They expressly admit (R. II, 1145), that "fair value" as used by them is their reproduction cost new estimate, less "observed depreciation", as determined by their

estimated "per cent condition", which quoted terms they erroneously treat as being synonymous with "accrued depreciation." They further testify that in arriving at their estimate of per cent condition they did not take into consideration any depreciation except that which was palpable to the eye by a casual inspection of the outside surfaces of the property, and that it was impossible to examine the interior of the property for any signs even of physical depreciation such as corrosion inside of pipe, R. II, 1197-1199, 1202, 1206. Much of the property was not even inspected by the Company's witnesses. Furthermore, their per cent condition totally ignored the intangible factors which bring about depreciation and ultimate retirement of property, and which intangible factors account for fully as much of the depreciation in the broader sense as does physical deterioriation. It was by this method that the Company arrived at its estimated over-all per cent condition of 94.26 per cent, R. II, 1145.

The Company used its "observed depreciation" of 5.74 per cent as being synonymous with "accrued depreciation"—whereas it is obvious that it does not represent, even approximately, the amount of actual accrued depreciation in the property, due to all causes, including physical deterioration, obsolescence, inadequacy, changed operating conditions, public requirements, etc.

Contrasted with this assumption is the inconsistent attitude of the Company in estimating its necessary annual accruals to the depreciation reserve. On that side of the ledger, getting away from the question of the rate base on which the Company should be al-

lowed to earn a return, and over on the side of where it was computing the money to be taken out of gross revenues for meeting current depreciation, Connor expressly took into consideration all causes, both observable and non-observable, which contributed to bring about depreciation in value and ultimate retirement.

The Company has not seen fit to provide for depreciation on its books at a rate more than approximately half of the annual rate estimated as necessary by Mr. Connor, R. III, 2140B, V, 3056. Yet the balance in the depreciation reserves stood at $15,695,413.00 on December 31, 1933, as compared with a book cost as of the same date of $50,283,644.00, (R. III, 2140A, 2140B), indicating an overall per cent condition of the property of 68.8%, or even less if any measure of credence is to be given Mr. Connor's estimate of the annual amount necessary to be set aside in the depreciation reserves. There is a complete disparity between Mr. Biddison's superficially observed per cent condition of 94.26% and Mr. Connor's estimate of the annual depreciation requirements.

We have in this brief adverted to only a relatively few of the countless glaring errors and inconsistencies on the part of the Company with which the whole record is shot through. It would be impossible in a brief any shorter than the record itself to point out all of these errors. We cite them, not always for the amount of money which they involve, nor for their glaring erroneousness, but simply as typical illustrations of methods used by the Company throughout this proceeding, from its inception.

NET RATE OF RETURN NECESSARY TO INSURE FINANCIAL SOUNDNESS OF THE COMPANY

The Commission aimed at fixing the rate at such a level as would bring the Company a net return of 6% for the basic year 1931, and would in average operation in the future (prospectively from September 13, 1933, the date of the order) yield a net average rate of return in excess of 6% per annum, over a reasonable spread of years, R. I, 111. The Commission computed return before federal income tax, R. I, 104. This rate of return was supported in the District Court by the testimony of a Commission witness (R. III, 1815-1816) as being sufficient to insure the credit and financial integrity of the Company, to induce a free flow of capital, and as being commensurate with the rates of net return being realized by utilities in the same general section of the country whose business was attended with like risk as that of the Company. Commission's witness Montgomery testified that over a period of ten years 5% net annual return would be a sufficient return, R. III, 1816, 1822.

The testimony in behalf of the Company was as follows: Connor testified that for the above purposes a net return of 10% per annum after federal income tax was necessary, R. II, 1330. Biddison testified that a minimum of 10% to a maximum of 15% after federal income tax was necessary, R. III, 2014-2015. An 8% minimum after depreciation and depletion (whether before or after federal income tax was not shown) was testified as necessary by banker Thornton, official of Mercantile National Bank of Dallas,

which bank had in the past made large loans to Appellant and had bought bonds issued by some of the Lone Star underlying companies, and which was one of the banks with which Appellant was doing business at the time of the trial; such loans to Appellant being made at 4% to 4½ % interest, R. III, 1963, 1964. The same testimony was given by Florence, an official of Republic National Bank of Dallas, which bank likewise had made loans to Appellant and which bank through Florence had participated in the successful sale of 5% debentures of Lone Star Gas Corporation, and which bank had also made loans upon the security of stock in the Lone Star Gas Corporation. This witness likewise testified that loans to Appellant were made at 4% to 4½ % interest per annum, R. III, 1965, 1967, 1974.

This is all to be contrasted with the Company's claim (p. 40 of its brief) that the actual rate of return being enjoyed by it *under the* 40c *rate* voluntarily fixed and adhered to by it for many years without even asking permission to raise the rate, was, for the years 1931 to 1934, only .61% to 1.71%. If as the Company's testimony would show, net returns of from 8% to 15% after federal income tax are necessary to enable the Company to survive and operate successfully, we can not understand how it could have survived as long as it has on such small rates of return as it claims to have been making under its 40c rate. It is enlightening to compare both the Company witnesses' testimony as to what rate of return is necessary for it to earn, and the Company's claims as to what net percentages it has actually been earning, with the percentages as found by the Commission as actually

earned in the past (1909-1931), the weighted average of which percentages (before annual depreciation) was 12.03% upon undepreciated book cost, R. I, 65. The Commission found slightly in excess of 2% for annual depreciation as applied to the undepreciated cost.

The record shows that in the past the Company has had a "free flow of capital" sufficient to meet all of its requirements, as and when needed, from the holding company at 6% interest, (R. I, 239), and short term loans from the above mentioned banks at 4% to 4½%, R. III, 1963-1974.

This Court has held in *Dayton P. & L. Co. vs. Pub. Utilities Co., supra,* that it would take judicial notice of economic conditions and consider them in deciding whether a particular rate of return was confiscatory. A 6½% return was upheld as being adequate in that case; and a 6% return was upheld in *Willcox vs. Consolidated Gas Co.,* 212 U. S. 91, 53 L. Ed. 382; *Cedar Rapids G. & L. Co. vs. Cedar Rapids,* 223 U. S. 655, 56 L. Ed. 594; *Des Moines Gas Co. vs. Des Moines,* 238 U. S. 153, 59 L. Ed. 1244. In *Knoxville vs. Knoxville Water Co.,* 212 U. S. 1, 17, 53 L. Ed. 371, 382, in periods of economic depression comparable to those which prevailed here, this Court refused to set aside as confiscatory a rate of 6% *before deduction of 2% for depreciation.*

Future Revenues: The year 1933 was the warmest year in the Company's history (R. III, 1595, 1895) and therefore the temperature adjustments made by the Commission's witness in the District Court, R. I, 389, 390; R. III, 1881, 1887, 1888,

1892, 1895, 1900, 2164-2173, were proper, as held by this Court in *Los Angeles G. & E. Co. vs. Railroad Commission of Cal.*, 58 Fed. (2d) 256, 286, aff. 289 U. S. 287, 298-300, 302, 303-304, 77 L. Ed. 1180, 1189-1190, 1191-1192, 1200.

It is shown at R. III, 1896, that the Company introduced, before the Commission, Weather Bureau records for years prior to the date of the Commission's hearing. It complains now, however, that similar data were introduced by the Commission in the District Court trial.

This Court has often taken judicial notice of economic conditions prevailing from time to time and, therefore, judicially knows the conditions which prevailed from 1931-1933. Specific data as to these trends, as applied to the Company's experience are shown in the record. The trend of both gross and net revenues was downward from 1931 to 1933 inclusive, R. I, 386. This was particularly true of industrial revenues, and the domestic revenues dropped off over $1,000,000.00 from 1932 to 1933, R. I, 385-387. Hulcy admits that the economic depression and the low temperatures of 1933 were contributing factors to these slumps, R. I,386-389; R. III. 1642. Connor claimed that the Company had shared with others this general business distress, R. II, 1448-1449. The securities market was pretty low when the Commission held its hearing (R. II, 1450) and was still lower at the time of the District Court trial, R. II, 1450-1451. The Company's operating statements show, however, that the trend of both gross and net revenues was upward during the first quarter of 1934. See Tables II and III, *infra;* and R. III, 1641.

COMPUTATIONS BY THE RESPECTIVE PARTIES OF NET RATES OF RETURN EARNED BY THE COMPANY IN PAST YEARS UNDER THE 40c RATE AND PROJECTION OF THE RATES OF RETURN PROBABLY TO BE EARNED IN THE FUTURE UNDER THE 32c GATE RATE

It is to be recalled that the Commission had before it operating statements for the six calendar years 1927-1932, and for the year ending April 30, 1933, R. I, 19-20, III, 1607. These were not submitted by the Company, however. The Company presented such statements for only the calendar years 1931 and 1932, and the overlapping year ending April 30, 1933, before the Commission. Before the Commission, however, the Appellees' accountant, Phillips, presented "accurate and detailed statements of revenues, expenses and book costs for the years 1927-1932, inclusive, as taken from the records of the Lone Star Gas Company", R. I, 18. The Commission used the year 1931 "as a basis for finding the city gate rate which would earn a fair return", R. I, 16. "This rate was then applied to the years 1927-1932 as a test of its reasonableness", R. I, 16.

Before the District Court the operating statements presented by the Company covered only the three calendar years 1931-1933, and the overlapping year ending March 31, 1934. Thus the Company was making an unwarranted attempt (*United Gas Pub. Serv. Co. vs. Texas*, ____ U. S. ____, 82 L. Ed.____, Adv. Op. No. 10, pp. 490, 500, 502, decided Feb. 14, 1938) to limit vision to a short period, affected deeply by the depression, including the year 1933,

which was the warmest year in the history of the Company, R. III, 1595, 1881-1895. Before the District Court, Appellees' accountant Phillips presented operating statements for the seven calendar years 1927-1933, and the overlapping year ending Mar. 31, 1934, (R. III, 2126A) giving the District Court a vision of average operations over a reasonable period of years.

The Company now complains bitterly of the temperature adjustments made for 1933 and the year ending Mar. 31, 1934, by Commission witness Freese, in the computations before the District Court, although the Company itself had introduced evidence and data on temperatures before the Commission, R. III, 1887, 1896. See Company's brief, p. 47; Appellees' Ex. 8, R. III, 2164-2165, 1896; specification of Error 15 (g), Company's brief, p. 58. This assignment ignores this Court's approval of the temperature adjustments similarly made in *Los Angeles G. & E. Corp. vs. R. R. Com. of Cal.*, 58 Fed. (2d) 256, 285, aff. 289 U. S. 287, 298-300, 303-304, 320, 77 L. Ed. 1180.

The Company in its brief has presented various computations of the net rates of return which it claims it has been earning under the 40c rate and which it claims it would earn under the 32c rate. None of these computations shows the rates of return which would be earned under the 32c rate by reason of the fact that each of such computations involves one or more of the following basic errors which should be borne in mind of the Court in its consideration of the claimed rates of return:

(a) Failure to use a sufficient spread of years to show average operating results leveling out the inevitable fluctuations due to all factors.

(b) Using the 40c rate instead of the 32c rate.

(c) Failing to make temperature corrections for the abnormal temperature periods.

(d) Failing to take into account the increased consumption which would result from putting the reduced rate into effect.

(e) Failing to take into account the increased consumption which will be certain to result in the future, from economic recovery.

(f) Using Connor's excessive deductions for depreciation and depletion requirements.

(g) Using the inflated rate bases as estimated by the Company witnesses.

(h) In not deducting the improper and questioned operating expenses referred to by us above.

(j) In cases where a depreciated rate base is used, in using too high a per cent condition of the property, which per cent condition does not take into account the various intangible factors of depreciation, such as obsolescence, inadequacy, changed operating conditions, depletion; and failure to depreciate all properly depreciable items such as rights-of-way, etc.

(k) Making computations of federal income tax which has never been incurred by the Company or paid to the government.

(l) Applying the Company's unacceptable basis of segregation between what it calls "interstate and intrastate operations".

The above *elements of error* are applied specifically to the various computations presented by the Company, by letter designation only, as follows:

In the computations at the bottom of page 39 and top of page 40 of Company's brief: a, b, c, d, e, f, g, h, j, k.

In the computations at page 41 of Company's brief: a, c, d, e, f, g, h, j.

In the second computations, page 41 of Company's brief, which apply to the Commission's findings: a, c, d, e, (h, in part), k.

In the computations at the top of page 42 of the Company's brief: a, c, d, e, h, k.

In the computations on pages 43-44 of Company's brief: a, c, d, e, g, h, j, k, l.

In the computations at top of page 60 of Company's brief: Same errors as are in computations on pp. 43-44.

In the computations at the top of page 156 of Company's brief: a, c, d, e, f, (h, in part) j.

In the computations at the bottom of page 156 of Company's brief: a, c, d, e, (h, in part) j.

In the computations at the bottom of page 157 of Company's brief: a, c, d, e, f, g, (h, in part) j.

In the computations at the top of page 158 of Company's brief: a, c, d, e, g, (h, in part) j.

In the computations at the middle of page 158 of Company's brief: a, c, d, e, (h, in part), k.

In the computations at the middle of page 159 of Company's brief: a, c, d, e, g, h, j, k, l.

In the computations at the middle of page 165 of Company's brief: a, c, d, e, (g, in part) h, k.

In the computations in the middle of page 167 of Company's brief: a, c, d, e, f, h, j.

In the computations at the bottom of page 167 of Company's brief: a, c, d, e, h, j.

In the computations at the middle of page 168 of Company's brief: a, c, d, e, f, g, h, j.

In the computations at the bottom of page 168 of Company's brief: a, c, d, e, g, h, j.

In the computations at the top of page 169 of Company's brief: a, c, d, e, f, g, h, j.

In the computations at the middle of page 169 of Company's brief: a, c, d, e, g, h, j.

In many instances Appellant purports in its computations to have applied the Commission's findings throughout; but an examination will reveal that it has not done so, at least in full. In each such case the Commission's findings are plain, and the Court by referring to such findings will discover wherein the Company has failed to apply or has mis-applied the Commission's findings.

We now come to the submission, for the Court's consideration, of our own computations of the rates of return which would be available to the Company under the 32c rate upon certain bases. We understand that we are under no legal duty to submit evidence or computations of our own in support of the compensatory character of the rate, and that if our own computations and evidence should not for any reason meet with the approval of the Court this still would not lift from Appellant the burden of proving the rate

confiscatory by clear and convincing proof of its own. But we desire to be of as much assistance to the Court as possible; hence we submit at the end of this brief our Tables I to V inclusive.

It is to be remembered that none of our said computations takes into account the increased consumption which would result from economic improvement or from actually putting the reduced rate into effect; nor do any of them take into account the deductions which should be made of the improper operating expenses which we have objected to above, with the exception of management fees, and in Tables II, III and V, of donations as shown.

Table I applies all of the Commission's findings throughout, except that we have made temperature corrections for 1933 as shown by the evidence adduced before the District Court. The Commission had evidence before it to show that the earlier years averaged out as normal so far as temperatures were concerned and, therefore, required no correction. This Table shows average net percentages of 8.00% and 9.16%, respectively, upon the bases there shown, for the seven years, 1927-1933, after application of the 32c gate rate. The percentages for 1927 to 1932, inclusive, are taken from the Commission's findings. It is to be noted that, in applying the Commission's findings to the year 1933, the rate base includes the net additions made during 1932 and 1933 at cost. These net additions comprise to a large extent the Southern Oil Production Properties and the properties of the Meridian Gas Company, which latter properties were purchased from the Lone Star Gas Corporation.

Table II is an application of the 32c gate rate to over-all Texas and Oklahoma operations, using undepreciated book cost and an undepreciated rate base as found by the Commission, respectively, and actual charges to the depreciation reserves, and shows an average of 8.72% and 8.82% upon the rate bases, respectively, for the seven years 1927-1933. In this connection it is well to recall the Company's complaint that the use of the actual charges to the depreciation reserves does not make any provision for the amortization of the Company's property at such time in the future as the natural gas supply may be exhausted. It will be remembered, however, that the record shows that .344% per annum (R. I. 97) will amortize the property over a period of fifty years on a 6% sinking fund basis. By deducting this percentage for amortization from the net percentages shown in Table II, there would be left 8.38% and 8.48%, as average returns for the seven year period on the undepreciated book cost and on the undepreciated rate base as found by the Commission, respectively. For the use of the actual charges to the depreciation reserves, see supra pp. 105, 106. Expenses as shown in the table (Table II) include the charging off on the books of the Company of large amounts for cancelled and surrendered leases, see supra pp. 122-124. It is to be noted that the book costs used in this table exceed the book costs claimed by the Company in amounts of approximately $450,000 to $675,000 for the years shown in the Company's exhibits, R. III, 2211, 2214, 2217. These book costs include the Petrolia Field account and the Meridian Gas Company properties, see supra pp. 154-156. The rate bases "as found by the Commission"

include the Southern Oil Production and the Meridian Gas Company properties at book cost. In comparing the book cost with the rate base found by the Commission, it should be remembered that a large part of the properties was built during peak-price periods, R. I. 109.

Table III applies the 32c gate rate to the undepreciated book cost on Texas properties and operations only, as segregated by the Commission's witness in the District Court trial, using average charges to the depreciation reserves, which shows an average net return of 8.18% over the five year period 1929-1933 inclusive. If the amortization allowance of .344% (R.I. 97) be deducted from this average it still leaves 7.84% return over the five year period as applied to the undepreciated book cost of the Texas properties. The same observations made with reference to Table II as to expenses and as to book costs are pertinent to Table III.

Table IV applies the 32c gate rate to the Texas properties and operations only, as per segregation submitted by the Commission's witness in the District Court trial, upon the undepreciated reproduction cost new as found by the Commission's witness, his allowance for depreciation being substantially the same as the allowance found by the Commission; using actual operating expenses as per the Company's books, except for management fees, as segregated by the Commission's witness in the District Court trial; and making temperature corrections for the calendar year 1933, and the year ending March 31, 1934. This table shows a rate of return of 6.72% for 1933 and 6.70%

for the year ending March 31, 1934. For the use of the prevailing wellhead price for Company produced gas in lieu of the inclusion of production expenses and production property, see supra pp. 143-156, especially 150-154.

Table V shows the application of the 32c gate rate to the "D" operations, which the Company admitted to be intrastate Texas operations, as per its totally unacceptable basis of segregation submitted in the District Court, and even this shows a return of **6.63%** applicable to "D" operations. As a basis for these computations, corrections for management fees, charitable donations and temperature adjustments have been made. Depreciation has been taken as estimated by Commission's witness. The rate base as determined by the Commission, plus net additions at cost as of December 31, 1933, has been used.

These tables show conclusively that the rate of return, based upon the 32c wholesale rate for domestic gas, would be substantially above the point of confiscation when tested in the light of a reasonable spread of years, either on the basis of the properties and operations as a whole or any segregation of the Texas properties and operations.

CONCLUSION

The financial history of the Company (R. I, 64-66) repels the suggestion that the Company has been operating under a confiscatory rate at 40c per MCF, as claimed by the Company at page 40 of its brief. On the contrary, the following table, taken from the Commission's findings, aforesaid, shows that the Company has been phenomenally successful and prosperous:

Period	Book Cost Public Service Property	Amount Available for Depreciation and Return	Per Cent of Undepreciated Book Cost	
June 4, 1909—May 31, 1910	$ 4,741,620.41	$ 57,607.99	1.21	
June 1, 1910—Feb. 28, 1911	4,790,284.17	160,761.86	3.35	(4.47 per annum)
Mar. 1, 1911—Feb. 28, 1912	4,994,064.08	610,992.63	12.23	
Mar. 1, 1912—Feb. 28, 1913	5,800,664.91	814,811.21	14.04	
Mar. 1, 1913—Feb. 28, 1914	6,164,123.74	1,114,369.22	18.08	
Mar. 1, 1914—Feb. 28, 1915	6,980,985.13	1,164,663.69	16.68	
Mar. 1, 1915—Dec. 31, 1915	7,715,247.24	736,351.36	9.54	(11.45 per annum)
1916	8,090,251.99	1,101,618.66	13.61	
1917	8,627,698.92	901,798.88	10.45	
1918	9,399,508.86	694,208.51	7.38	
1919	12,749,862.20	1,032,035.11	8.09	
1920	16,225,774.18	1,227,479.44	7.38	
1921	16,336,266.61	1,331,944.53	8.15	
1922	17,572,198.80	1,677,754.21	9.54	
1923	18,870,227.60	2,232,771.43	11.83	
1924	20,281,257.29	2,843,831.77	14.02	
1925	24,294,693.33	3,950,790.60	16.26	
1926	25,113,114.07	4,334,870.94	17.26	
1927	33,307,350.60	4,513,876.52	13.55	
1928	36,879,954.99	5,028,295.46	13.63	
1929	44,449,143.87	5,869,183.24	13.20	
1930	47,703,209.28	5,297,491.90	11.10	
1931	47,776,749.63	4,605,721.83	9.64	

The foregoing tabulation reflects a weighted average annual rate of return on the undepreciated book cost, of 12.03%, before depreciation, R. I, 65.

While it may be true that on certain minor, subsidiary issues the evidence was conflicting, still after considering the many liberalities of the Commission, and setting them off against any possible elements as to which a conflict of evidence may have created a doubt as to sufficiency, (See Point XXXIII, pp. 90-91, *infra*, and cases cited), and considering the insufficiency of Appellant's evidence as a whole (the totality of its consequences), it is clear that no issue or issues as to confiscation were raised which required submission to the jury. Although the burden has not been upon the Commission at any stage of the proceedings to

submit any evidence in support of the rate fixed, yet, we submit that under the evidence voluntarily produced by the Commission the rate has affirmatively been shown to be compensatory. The correctness of the findings of the Commission has not been refuted by the Company's evidence, but on the contrary has been supported by the evidence. A reading of the Commission's opinion, (R. I, 12-116) and the opinion of the Court of Civil Appeals, (R. V, 3333-3370) will show that the Commission was in many respects very much more liberal with the Company than it was required by law to be, and if the Commission's findings are applied it is demonstrated beyond all cavil that the rate is compensatory.

We submit that under the authorities cited under our Point XLI, pp. 97-98 *supra*, the Company's evidence has "proved too much" and "over-shot the mark," and "must fail of the intended effect".

We, therefore, pray, that the judgment of the Court of Civil Appeals and of the Supreme Court of Texas be affirmed.

Respectfully submitted,

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Attorney General of Texas

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of Texas

EDWARD H. LANGE,
Laredo, Texas
Counsel for Appellees

TABLES I TO V INCLUSIVE:

TABLE I
Texas and Oklahoma Operations
RETURN BASED ON COMMISSION FINDINGS
32c GATE RATE

Year	Excluding Earnings From Government and Northern Natural Including Production Properties Undepreciated Rate Base		Including Earnings From Government and Northern Natural Gas at Wellhead at Prevailing Field Price Undepreciated Rate Base	
1927	11.42%	(1)	12.62%	(3)
1928	9.70%	(1)	10.90%	(3)
1929	9.83%	(1)	11.03%	(3)
1930	7.46%	(1)	8.66%	(3)
1931	6.02%	(1)	7.22%	(3)
1932	6.34%	(1)	7.54%	(3)
1933	5.20%	(2)	6.16%	(4)
Average	8.00%		9.16%	

Reference:

(1) R. I, 20, 111.

(2) Available for Federal Income Tax and Return ..... $2,070,006.97 - R. III, 2284
Temperature Correction ..... 441,240.12 - R. III, 2164

$2,511,247.09

Rate Base—As found by Commission at Dec. 31, 1931, plus net additions at cost ..... $48,306,893.96 R. III, 2285

Available for Return—
Per Cent of Rate Base 5.20%

For temperature data before Commission see R. III, 1881.
For Commission Findings as to Federal Income Tax see R. I, 104, 105.

(3) R. I, 20, 114.

(4) 5.20% from first column plus .96% making a total of 6.16%.
For .96% see R. I, 114.

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TABLE II
Texas and Oklahoma Operations
BASED ON 32c GATE RATE
(Actual Charges to Depreciation Reserves—Average for 7 Yrs.)

	References to Calculations	For the year ended: 12-31-1927	12-31-1928	12-31-1929	12-31-1930	12-31-1931	12-31-1932	12-31-1933	3-31-1934 (9 mo. overlap with last period)
Revenues: R. III, 2126A		$ 9,020,274.96	$ 9,541,976.32	$11,886,128.49	$10,752,143.01	$ 9,301,862.65	$ 8,859,188.20	$ 7,728,309.05	$ 7,965,978.89
Amount of 8c per MCF Reduction: R. III, 2126B	(1)	973,702.96	1,199,373.20	1,414,553.76	1,437,941.36	1,361,894.96	1,332,135.04	1,115,586.64	1,151,152.40
Revenues at 32c Domestic Gate Rate		8,046,572.00	8,342,603.12	9,671,574.73	9,314,201.65	7,939,967.69	7,527,053.16	6,612,722.41	6,814,826.49
Expenses (Less Management Fees and Donations): R. III, 2126A, 2131, 2132	(2)	3,979,878.47	3,972,592.29	4,640,581.22	4,923,066.76	4,291,467.47	3,751,172.07	3,517,900.39	3,491,368.82
Available for Return, Depreciation, and Federal Income Tax		4,066,693.53	4,370,010.83	5,031,201.51	4,391,134.89	3,648,500.22	3,775,881.09	3,094,822.02	3,323,457.67
Average Depreciation Reserve Charges: R. III, 2140B	(3)	344,871.84	344,871.84	344,871.84	344,871.84	344,871.84	344,871.84	344,871.84	344,871.84
Available for Return and Federal Income Tax		3,721,821.69	4,025,138.99	4,686,329.67	4,046,263.05	3,303,628.38	3,431,009.25	2,749,950.18	2,978,585.83
Federal Income Tax	(4)	188,810.12	188,343.99	233,856.45	124,376.47	25,280.18	18,319.40		
Available for Return		3,533,011.57	3,836,795.10	4,454,473.22	3,921,886.58	3,278,348.20	3,412,689.85	2,749,950.18	2,978,585.83
Book Cost: R. III, 2140A	(5)	29,517,879.08	33,461,928.96	41,340,023.12	46,745,646.84	48,409,802.24	49,484,864.66	50,399,110.82	50,399,110.82
Return on Undepreciated Book Cost		11.97%	10.76%	10.78%	8.39%	6.77%	6.90%	5.46% (a)	5.91% (a)
					(Average 1927-1933 inc.: 8.72%)				
Rate Base as found by R. R. Comm.: R. I, 110, III, 2285	(6)	29,517,879.08	33,461,928.96	41,340,023.12	46,745,646.84	46,246,617.53	48,304,299.60	48,306,893.96	48,342,628.99
Return on Rate Base found by R. R. Comm.: (Undepreciated)		11.97%	10.76%	10.78%	8.39%	7.09%	7.04%	5.69% (b)	6.16% (b)
					(Average 1927-1933 inc.: 8.82%)				

Note (a): No temperature correction made for these abnormal periods. Correction to normal temperature basis would raise return for 1933 to 6.34% and for year ended 3-31-1934, to 6.44%. R. III, 2164-2173 inc.
Note (b): With temperature correction return for 1933 would have been 6.60% and for year ended 3-31-1934, 6.72%. R. III, 2164-2173 inc.

References to Calculations

(1) See State Exhibit No. 5—R. III, 2126B for Total Domestic Gas Sales

Twelve months ended		
12-31-1927	12,171,287 MCF @ 8c	$ 973,702.96
12-31-1928	14,992,165 MCF @ 8c	1,199,373.20
12-31-1929	17,681,922 MCF @ 8c	1,414,553.76
12-31-1930	17,974,267 MCF @ 8c	1,437,941.36
12-31-1931	17,023,687 MCF @ 8c	1,361,894.96
12-31-1932	16,651,688 MCF @ 8c	1,332,135.04
12-31-1933	13,944,833 MCF @ 8c	1,115,586.64
3-31-1934	14,389,405 MCF @ 8c	1,151,152.40

(2) Expenses (Less Management Fees and Donations): State Exhibit No. 5, R. III, 2126A, 2131, 2132

Twelve months ended	Expenses other than Gas Production and Management Fees R. III, 2126A	Gas Production Expenses and Management Fees R. III, 2126A	Total Expenses Including Management Fees and Donations Calculated	Management Fees R. III, 2126A	Donations R. III, 2131 R. III, 2132	Total Management Fees and Donations Calculated	Expenses Less Management Fees and Donations Calculated
12-31-1927	$3,874,820.10	$118,699.12	$3,993,519.22	----------	$ 13,640.75	$ 13,640.75	$3,979,878.47
12-31-1928	3,912,327.85	79,093.89	3,991,421.74	----------	18,829.45	18,829.45	3,972,592.29
12-31-1929	4,586,817.82	181,709.73	4,768,527.55	95,062.03	32,884.30	127,946.33	4,640,581.22
12-31-1930	4,590,035.27	467,233.64	5,057,268.91	105,625.72	28,576.43	134,202.15	4,923,066.76
12-31-1931	3,926,629.11	466,062.41	4,392,691.52	91,375.38	9,848.67	101,224.05	4,291,467.47
12-31-1932	3,445,049.84	403,661.87	3,848,711.71	87,197.87	10,341.77	97,539.64	3,751,172.07
12-31-1933	3,270,595.62	333,917.07	3,604,512.69	75,940.60	10,671.70	86,612.30	3,517,900.39
12-31-1934	3,260,886.27	318,798.38	3,579,684.65	78,294.78	10,021.05	88,315.83	3,491,368.82

(3) For Charges to Depreciation Reserves see State Exhibit No. 5 R. III, 2140B

Twelve months ended	Charges to Reserves
12-31-1927	$245,097.73
12-31-1928	260,768.59
12-31-1929	450,335.00
12-31-1930	464,875.93
12-31-1931	720,014.28
12-31-1932	-62,725.18
12-31-1932	335,736.55
Average	$344,871.84

(4) Per Federal Income Tax Rates see R. III, 2296
Per 5% of Book Cost for Depreciation Allowance for Federal Income Tax see R. III, 1889, I, 399-400.
Per Interest Payments see R. III, 2296, I, 412. 1927 to 1930 inclusive taken at amount paid in 1931

Twelve months ended	Amount available for Return, Depreciation and Federal Income Tax	Estimated Depreciation Allowance for Federal Income Tax	Interest Payments	Net Amount After Depreciation Allowance and Interest	Federal Income Tax Rate	Computed Federal Income Tax

(5) Average Book Cost for each year as taken from State Exhibit No. 5 R. III. 2140A

Twelve months ended	Book Cost At Beginning of Period	Book Cost At End of Period	Average for Period
12-31-1927	$25,263,504.93	$33,772,253.23	$29,517,879.08
12-31-1928	33,772,253.23	37,551,604.69	35,661,928.96
12-31-1929	37,551,604.69	45,128,441.56	41,340,023.12
12-31-1930	45,128,441.56	48,362,852.13	46,745,646.84
12-31-1931	48,362,852.13	48,455,152.34	48,409,002.24
12-31-1932	48,455,152.34	50,514,576.98	49,484,864.66
12-31-1933	50,514,576.98	50,283,644.65	50,399,110.82
3-31-1934	.....	50,325,548.93	50,399,110.82 (1933)

(6) Years 1927-1930 inclusive taken from R. I. 110
Years 1931-1933 inclusive and year ended 3-31-1934, taken from R. III. 2285
(The Railroad Commission found a reproduction cost new less than the book cost for 1931, but adopted the book cost for 1927-1930, inclusive.)

TABLE III
Texas Operations
BASED ON 32c GATE RATE
(Average Charges to Depreciation Reserves)

	Reference to Calculations	For the year ended: 12-31-1929	12-31-1930	12-31-1931	12-31-1932	12-31-1933	3-31-1934 (9 mo. overlap with last period)
Revenues: R. III, 2116A		$10,715,994.70	$10,379,829.27	$ 8,938,441.77	$ 8,503,942.21	$ 7,423,680.87	$ 7,663,061.50
Amount of 8c per MCF Reduction: R. III, 2116B	(1)	1,360,932.16	1,382,222.48	1,307,523.20	1,277,684.48	1,070,458.16	1,106,537.68
Revenues at 32c Domestic Gate Rate		9,355,062.54	8,997,606.79	7,630,918.57	7,226,257.73	6,353,222.71	6,556,523.82
Expenses (Less Management Fees and Donations): R. III, 2116A, 2123, 2124	(2)	5,013,566.92	5,018,235.74	4,081,951.56	3,527,505.03	3,154,644.52	3,161,055.66
Available for Return, Depreciation and Federal Income Tax		4,341,495.62	3,979,371.05	3,548,967.01	3,698,752.70	3,198,578.19	3,395,468.16
Average Depreciation Reserve Charges: R. III, 2140B	(3)	296,589.78	296,589.78	296,589.78	296,589.78	296,589.78	296,589.78
Available for Return and Federal Income Tax		4,044,905.84	3,682,781.27	3,252,377.23	3,402,162.92	2,901,988.41	3,098,878.38
Federal Income Tax	(4)	198,149.52	126,226.77	65,565.61	67,545.92	7,917.69	37,209.47
Available for Return		3,846,756.32	3,556,554.50	3,186,811.62	3,334,617.00	2,894,070.72	3,061,668.91
Book Cost: R. III, 2125	(5)	36,306,022.53	41,050,656.27	42,552,769.02	44,053,612.30	44,053,612.30	44,053,612.30
Return on Undepreciated Book Cost		10.60%	8.66%	7.49%	7.57%	6.57% (a)	6.95% (a)

(Average 1929-1933 inc.: 8.18%)

Note (a) No temperature correction made for these abnormal periods. Correction to normal temperature basis would raise return for 1933 to 7.43% and for year ended 3-31-1934 to 7.48%. R. III, 2164-2173 inc.

References to Calculations

(1) See State Exhibit No. 4, R. III, 2116B for Total Domestic Sales:

Twelve months ended		
12-31-1929	17,011,652 MCF @ 8c	$1,360,932.16
12-31-1930	17,277,781 MCF @ 8c	1,382,222.48
12-31-1931	16,344,040 MCF @ 8c	1,307,523.20
12-31-1932	15,971,056 MCF @ 8c	1,277,684.48
12-31-1933	13,380,727 MCF @ 8c	1,070,458.16
3-31-1934	13,831,721 MCF @ 8c	1,106,537.68

(2) Expenses (Less Management Fees and Donations) State Exhibit No. 4, R. III, 2116A, 2123, 2124

Twelve months ended	Expenses other than Gas Production and Management Fees R. III, 2116A	Gas Production Expenses and Management Fees R. III, 2116A	Total Expenses Including Management Fees and Donations Calculated	Management Fees R. III, 2116A	Donations R. III, 2123 R. III, 2124	Total Management Fees and Donations Calculated	Expenses Less Management Fees and Donations Calculated
12-31-1929	$4,965,432.99	$170,881.77	$5,136,314.76	$ 92,020.05	$ 30,727.79	$122,747.84	$5,013,566.92
12-31-1930	4,727,647.49	419,455.97	5,147,103.46	102,074.67	26,793.05	128,867.72	5,018,235.74
12-31-1931	3,727,634.84	452,092.47	4,179,727.31	87,926.88	9,848.87	97,775.75	4,081,951.56
12-31-1932	3,253,594.95	368,049.70	3,621,644.65	83,797.85	10,341.77	94,139.62	3,527,505.03
12-31-1933	2,932,557.52	305,795.87	3,238,353.39	73,037.17	10,671.70	83,708.87	3,154,644.52
3-31-1934	2,948,324.05	298,165.71	3,246,489.76	75,413.05	10,021.05	85,434.10	3,161,055.66

(3) Charges to Depreciation Reserves R. III, 2140B. Average for Texas and Oklahoma properties for 1927-1933, inclusive: $344,871.84. Factor of .86 used to arrive at average charges for Texas properties only. For .86 factor see R. III, 1748.
$344,871.84 @ .86=$296,589.78

(4) For Federal Income Tax Rates see R. III, 2296
For Est. of Book Cost for Depreciation Allowance for Federal Income Tax see R. III, 1889, I, 399, 400, III, 1879
For Interest Payments see R. III, 2296, I, 412; 1929 and 1930 taken at amount of interest paid in 1931.

[illegible]	[illegible]	Estimated Depreciation Allowance for Federal Income Tax	Interest Payments @ .86 as applicable to Texas	Net Amount After Depreciation Allowance and Interest	Federal Income Tax Rate	Computed Federal Income Tax
[illegible]	$4,341,495.62	$1,815,301.13	$ 874,948.47	$1,651,246.02	12.00%	$198,149.52
[illegible]	3,979,371.05	2,052,532.81	874,948.47	1,051,889.77	12.00%	126,226.77
[illegible]	3,548,967.01	2,127,638.45	874,948.47	546,380.09	12.00%	65,565.61
[illegible]	3,698,752.70	2,202,680.61	1,004,829.03	491,243.06	13.75%	67,545.92
12-31-1933	3,198,578.19	2,202,680.61	938,314.35	57,583.23	13.75%	7,917.69
3-31-1934	3,395,468.16	2,202,680.61	922,173.21	270,614.34	13.75%	37,209.47

[illegible] 12-31-1931 Book Cost $42,552,769.02 3-31-34

Twelve months ended	Amount Available for Return, Depreciation and Federal Income Tax	Estimated Depreciation Allowance for Federal Income Tax	Interest Payments @ .86 as applicable to Texas	Net Amount After Depreciation Allowance and Interest	Federal Income Tax Rate	Computed Federal Income Tax
12-31-1929	$4,341,495.62	$1,815,301.13	$ 874,948.47	$1,651,246.02	12.00%	$198,149.52
12-31-1930	3,979,371.05	2,052,532.81	874,948.47	1,051,889.77	12.00%	126,226.77
12-31-1931	3,548,967.01	2,127,638.45	874,948.47	546,380.09	12.00%	65,565.61
12-31-1932	3,698,752.70	2,202,680.61	1,004,829.03	491,243.06	13.75%	67,545.92
12-31-1933	3,198,578.19	2,202,680.61	938,314.35	57,583.23	13.75%	7,917.69
3-31-1934	3,395,468.16	2,202,680.61	922,173.21	270,614.34	13.75%	37,209.47

(5) From State Exhibit No. 4 R. III. 2125. Book Cost Texas Properties 3-31-34: $44,053,612.30. 12-31-1931 Book Cost: $42,552,769.02. 3-31-34 Cost used for 1932, 1933 and year ended 3-31-34. 12-31-1931 Cost used for 1931. 1930 Cost taken at 96.47% of 12-31-1931 Cost. 1929 Cost taken at 85.32% of 12-31-1931 Cost. For 1929 and 1930 ratios to 12-31-1931 Cost see Book Cost for overall properties in Table I.

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TABLE IV

Texas Properties

TAKEN FROM STATE'S EXHIBIT 8 (R. III, 2164)

Amount Available for Return at 32c Domestic Gate Rate after Correction to Normal Temperatures Years ending Dec. 31, 1933 and March 31, 1934.

Revenues	Year Ending 3-31-34	12-31-33
Revenues @ 40c Domestic Gate Rate	$7,663,034.50	$7,423,680.87
Amount of 8c Domestic Gate Rate Reduction	1,106,537.68	1,070,458.16
Revenues @ 32c Domestic Gate Rate	$6,556,496.82	$6,353,222.71
Expenses		
Gas Purchased	$1,073,493.16	$1,071,170.87
Gathering Expenses	96,589.70	95,911.08
Compressing Station Expenses	310,679.12	303,454.78
Transmission System Expenses	368,419.03	374,275.77
General Expenses	733,121.58	754,282.79
Taxes other than Gross Production and Federal Income Taxes	295,218.11	295,218.11
Auto and Truck Expenses—Underdistributed	3,221.27	3,223.15
Bad Debts and Adjustments	5,155.29	5,210.33
Miscellaneous Non-Operating Expenses	192.72	192.72
Texas-Oklahoma Gas Sales Adjustment	62,234.07	29,617.92
	$2,948,324.05	$2,932,557.52
	$3,608,172.77	3,420,665.19
Depreciation	831,946.08	831,946.08
	$2,776,226.69	$2,558,719.11
Value of Company Produced Gas	232,644.75	212,031.46
	$2,543,581.94	$2,376,687.65
Temperature Correction	268,829.64	441,240.12
	$2,812,411.58	$2,817,927.77
Federal Income Tax	97,534.45	96,073.64
	$2,714,877.13	$2,721,854.13
Return on $40,256,862.39 (R. III, 2143)	6.74%	6.76%
After correction allowance of $16,500 additional for depreciation: Return on $40,256,862.39	6.70%	6.72%

(R. III, 1900)

TABLE V
RETURN BASED ON COMPANY'S SEGREGATION AFTER GIVING EFFECT TO 32c GATE RATE YEAR 1933 ONLY

	Total	Applicable to "D" Operations (West Texas Gas)
Amount Available for Depreciation and Return (1)	$ 3,000,493.28	
Management Fees (2)	75,940.60	
Charitable Donations (2)	10,671.70	
Corrected Amount Available for Depreciation and Return	$ 3,087,105.58	
Temperature Correction (3)	441,240.12	
	$ 3,528,345.70	
Depreciation (4)	848,446.08	
Available for Return	$ 2,679,899.62	
Rate Base by Commission Plus Net Additions at Cost (5)	$48,306,893.96	
Return	5.55%	6.63% [6]

(1) From Company Exhibit 46, R. V, 3288.
(2) Not properly included in Operating Expenses, R. III, 2228.
(3) R. III, 2164. (This correction covers Texas operations only).
(4) Table IV, infra. ($831,946.08 plus $16,500)
(5) R. III, 2285.
(6) In Same Proportions as in Company Exhibit 46, R. III, 3288.

APPENDIX A

(Revised Civil Statutes, Texas, 1925)

Art. 6050. Classification.

The term "gas utility" and "public utility" or "utility," as used in this subdivision, means and includes persons, companies and private corporations, their lessees, trustees, and receivers, owning, managing, operating, leasing or controlling within this State any wells, pipe lines, plant, property, equipment, facility, franchise, license, or permit for either one or more of the following kinds of business:

1. Producing or obtaining, transporting, conveying, distributing or delivering natural gas: (a) for public use or service for compensation; (b) for sale to municipalities or persons or companies, in those cases referred to in paragraph 3 hereof, engaged in distributing or selling natural gas to the public; (c) for sale or delivery of natural gas to any person or firm or corporation operating under franchise or a contract with any municipality or other legal subdivision of this State; or, (d) for sale or delivery of natural gas to the public for domestic or other use.

2. Owning or operating or managing a pipe line for the transportation or carriage of natural gas, whether for public hire or not, if any part of the right of way for said line has been acquired, or may hereafter be acquired by the exercise of the right of eminent domain; or if said line or any part thereof is laid upon, over or under any public road or highway of this State, or street or alley of any municipality, or the right of way of any railroad or other public utility; including

also any natural gas utility authorized by law to exercise the right of eminent domain.

3. Producing or purchasing natural gas and transporting or causing the same to be transported by pipe lines to or near the limits of any municipality in which said gas is received and distributed or sold to the public by another public utility or by said municipality, in all cases where such business is in fact the only or practically exclusive agency of supply of natural gas to such utility or municipality, is hereby declared to be virtual monopoly and a business and calling affected with a public interest, and the said business and property employed therein within this State shall be subject to the provisions of this law and to the jurisdiction and regulation of the Commission as a gas utility.

Every such gas utility is hereby declared to be affected with a public interest and subject to the jurisdiction, control and regulation of the Commission as provided herein.

Art. 6051. *May enjoin gas pipe line.*

The operation of gas pipe lines for buying, selling, transporting, producing or otherwise dealing in natural gas is a business which in its nature and according to the established method of conducting the business is a monopoly and shall not be conducted unless such gas pipe line so used in connection with such business be subject to the jurisdiction herein conferred upon the Commission. The Attorney General shall enforce this provision by injunction or other remedy.

Art. 6053. *Regulation of utilities.*

The Commission after due notice shall fix and establish and enforce the adequate and reasonable

price of gas and fair and reasonable rates of charges and regulations for transporting, producing, distributing, buying, selling and delivering gas by such pipe lines in this State; and shall establish fair and equitable rules and regulations for the full control and supervision of said gas pipe lines and all their holdings pertaining to the gas business in all their regulations to the public, as the Commission may from time to time deem proper; and establish a fair and equitable division of the proceeds of the sale of gas between the companies transporting or producing the gas and the companies distributing or selling it; and prescribe and enforce rules and regulations for the government and control of such pipe lines in respect to their gas pipe lines and producing, receiving, transporting and distributing facilities; and regulate and apportion the supply of gas between towns, cities, and corporations, and when the supply of gas controlled by any gas pipe line shall be inadequate, the Commission shall prescribe fair and reasonable rules and regulations requiring such gas pipe lines to augment their supply of gas, when in the judgment of the Commission it is practicable to do so; and it shall exercise its power, whether upon its own motion or upon petition by any person, corporation, municipal corporation, county, or commissioner's precinct showing a substantial interest in the subject, or upon petition of the Attorney General, or of any county or district attorney in any county wherein such business or any part thereof may be carried on.

Art. 6054. *Orders, etc. reviewed.*

All orders and agreements of any company or corporation or any person or persons controlling such pipe lines establishing and prescribing prices, rates, rules and regulations and conditions of

service, shall be subject to review, revision and regulation by the Commission on hearing after notice as provided for herein to the person, firm, corporation, partnership or joint stock association owning or controlling or operating the gas pipe line affected.

Art. 6055. To refund excess charges.

If any rate or charge for gas or for service or for meter rental or any other purpose pertaining to the operation of said business shall be made or promulgated by any person, firm or corporation owning or operating any gas pipe line, or in the event of an inadequate supply of gas or inadequate service in any respect, and complaint against same shall be filed by any person authorized by the preceding article to file such petition and such complaint is sustained in whole or in part, all persons and customers of said gas pipe line shall have the right to reparation or reimbursement of all excess in charges so paid over and above the proper rate or charge as finally determined by the Commission from and after the date of the filing of such complaint.

Art. 6058. Appeal from City Control.

When a city government has ordered any existing rate reduced, the gas utility affected by such order may appeal to the Commission by filing with it on such terms and conditions as the Commission may direct, a petition and bond to review the decision, regulation, ordinance, or order of the city, town or municipality. Upon such appeal being taken the Commission shall set a hearing and may make such order or decision in regard to the matter involved therein as it may deem just and reasonable. The Commission shall

hear such appeal de novo. Whenever any local distributing company or concern, whose rates have been fixed by any municipal government, desires a change of any of its rates, rentals or charges, it shall make its application to the municipal government where such utility is located and such municipal government shall determine said application within sixty days after presentation unless the determination thereof may be longer deferred by agreement. If the municipal government should reject such application or fail or refuse to act on it within said sixty days, then the utility may appeal to the Commission as herein provided. But said Commission shall determine the matters involved in any such appeal within sixty days after the filing by such utility of such appeal with said Commission or such further time as such utility shall in writing agree to, but the rates fixed by such municipal government shall remain in full force and effect until ordered changed by the Commission.

Art. 6059. *Appeal from orders.*

If any gas utility or other party at interest be dissatisfied with the decision of any rate, classification, rule, charge, order, act or regulation adopted by the Commission, such dissatisfied utility or party may file a petition setting forth the particular cause of objection thereto in a court of competent jurisdiction in Travis County against the Commission as defendant. Said action shall have precedence over all other causes on the docket of a different nature and shall be tried and determined as other civil causes in said court. Either party to said action may have the right of appeal; and said appeal shall be at once returnable to the appellate court, and said action so appealed shall have precedence in said appellate court of all causes

of a different character therein pending. If the court be in session at the time such right of action accrues, the suit may be filed during such term and stand ready for trial after ten days notice. In all trials under this article the burden of proof shall rest upon the plaintiff, who must show by clear and satisfactory evidence that the rates, regulations, orders, classifications, acts or charges complained of are unreasonable and unjust to it or them.